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IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

WILLIE A. ANDERSON,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

FILED

OCT 25 1968

WM. B. LUCK, CLERK

APPELLEE'S BRIEF

NOV 1 1968

APPEAL FROM  
THE UNITED STATES DISTRICT COURT  
FOR THE CENTRAL DISTRICT OF CALIFORNIA

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APPELLEE'S BRIEF

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CONCLUSION  
APPEAL FROM  
THE UNITED STATES DISTRICT COURT  
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APPELLEE'S BRIEF

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I

STATEMENT OF ISSUES

Defendant's brief raises the following issues:

1. Did the trial court commit prejudicial error in not conducting a hearing outside the presence of the jury to determine whether the in-court identification of defendant and co-defendant by witnesses Paley, Branning and Hernandez were tainted by the pretrial viewing of photographs depicting defendant and co-defendant in the absence of defendant's counsel?
2. Was the manner of exhibiting the photographs of defendant and co-defendant to witnesses Paley and Hernandez so



defective so as to deprive the defendant of due process of law?

## II

### STATEMENT OF FACTS

WILLIE A. ANDERSON and a co-defendant were indicted on May 3, 1967, for violations of Title 18, United States Code, Section 371 (conspiracy to defraud the United States) and Section 472 (uttering counterfeit obligations) [R. T. 9-13]. <sup>1/</sup> The eight count Indictment charged ANDERSON and a co-defendant with one count (Count One) of conspiring to pass counterfeit \$10.00 Federal Reserve Notes and five counts (Counts Two through Six) of passing counterfeit \$10.00 Federal Reserve Notes.

ANDERSON was arraigned and entered a plea of not guilty to all counts on May 15, 1968. Prior to trial, the Government dismissed Count Two of the Indictment and at the conclusion of the Government's case, the Court ordered, as to Count One, a judgment of acquittal [R. T. 14-15, 165]. Trial by jury commenced on August 1, 1968, before the Honorable Warren J. Ferguson, United States District Judge [R. T. 4]. A verdict of guilty on Counts Three and Six was returned on August 2, 1968 [R. T. 243]. On September 15, 1967, ANDERSON was sentenced to the custody of the Attorney General for a period of five years [R. T. 264].

---

1/ "R. T." refers to Reporter's Transcript.



III

ARGUMENT

A. DEFENDANT CANNOT RAISE ON APPEAL  
A POINT NOT URGED IN THE TRIAL  
COURT.

---

Defendant ANDERSON contends that he was entitled to have had the trial judge conduct a hearing outside the presence of the jury to determine whether the in-court identifications by witnesses Paley, Branning and Hernandez were tainted by a pretrial photographic display.

Defendant was represented by competent counsel at trial. No testimony was offered at trial which in any way showed that the pretrial photographic display was unnecessarily suggestive, and no issue was raised by defendant during trial that this procedure was conducted in a prejudicial manner. Having failed to raise this issue in the trial court, defendant should not be allowed to raise it for the first time in this Court. See United States v. Ladson, 294 F. 2d 535, 538 (2nd Cir. 1961), cert. denied 369 U. S. 824 (1962); Rugendorf v. United States, 376 U. S. 528 (1963), reh. denied 377 U. S. 940 (1964); Williams v. United States, 358 F. 2d 325 (9th Cir. 1966).



B. THE RIGHT TO COUNSEL AT PRETRIAL LINEUPS DOES NOT EXTEND TO PRE-TRIAL PHOTOGRAPH IDENTIFICATION.

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Defendant's contention that he was entitled to have his counsel present at a pretrial photographic display is based upon extension of the rule established in United States v. Wade, 388 U.S. 218, wherein the Court held that the accused is entitled to counsel at all critical stages of the criminal prosecution and that a pretrial lineup at which the accused is exhibited to identifying witnesses is a critical stage of the criminal prosecution. The Court, however, in the Wade case, clearly distinguished pretrial lineups from other stages in the criminal prosecution of a less critical nature, ". . . such as systematized or scientific analyzing of the accused's fingerprints, blood sample, clothing, hair and the like". See Wade, supra, at p. 227. The Court explained this distinction as follows:

"We think there are differences which preclude such stages being characterized as critical stages at which the accused has the right to the presence of his counsel. Knowledge of the techniques of science and technology is sufficiently available, and the variables in techniques few enough, that the accused has the opportunity for a meaningful confrontation of the Government's case at trial through the ordinary processes of cross-examination of the Government's expert witnesses and the



presentation of the evidence of his own experts.

The denial of a right to have his counsel present at such analyses does not therefore violate the Sixth Amendment; they are not critical stages since there is minimal risk that his counsel's absence at such stages might derogate from his right to a fair trial."

Wade, supra, at pp. 227-228.

This distinction was applied in United States v. Miller,  
\_\_\_\_ F. Supp. \_\_\_\_ (D. C. E. D. Penn. 1968) (No. 22960, Sept. 3, 1968), wherein the Court held that pretrial photographic displays are not a critical stage in the criminal prosecution and therefore the accused is not entitled to have his counsel present when such displays are conducted. The Court reasoned in the Miller case that any form of unfair suggestion or other prejudice at this procedure ". . . arises from the nature and/or type of photographs displayed. By using these photographs in his cross-examination of Government witnesses, defense counsel easily can reveal such prejudice and thereby impugn the related identification testimony". See Miller, supra, at p. 3256.

C. THE MANNER IN WHICH THE PRE-TRIAL PHOTOGRAPHIC DISPLAY WAS CONDUCTED DID NOT DENY APPELLANT DUE PROCESS OF LAW.

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Defendant contends that Special Agent Tomsic displayed



photographs, including his photograph, to witnesses Paley, Branning and Hernandez in an unnecessarily suggestive manner. Defendant further argues that this procedure was conductive to irreparable mistaken identification and therefore all identification testimony at trial of these witnesses who viewed the photographs should have been suppressed.

The question of whether defendant's photographic identification constituted a denial of his right to due process of law depends on the circumstances surrounding the photographic display. Stovall v. Denno, 388 U.S. 293 (1968). As stated in Simmons v. United States, 390 U.S. 377 (1968) at page 384:

" . . . we hold that each case must be considered on its own facts, and that convictions based on eyewitness identification at trial following a pretrial identification by photograph will be set aside on that ground only if the photographic identification procedure was so impermissibly suggestive as to give rise to a very substantial likelihood of irreparable misidentification. This standard accords with our resolution of a similar issue in Stovall v. Denno, 388 U.S. 293, 301-302, and with decisions of other courts on the question of identification by photograph."

See also People v. Evans, 39 Cal. 2d 242, 246 P. 2d 636.



The evidence in this case discloses that witnesses Paley, Branning and Hernandez were shown between eight and ten photographs at a pretrial photographic display a week before defendant's trial began [R. T. 64-69, 88-90, 115-119]. Of these, approximately three were of defendant and three were of co-defendant Miller. It is not clear from the record whether the remaining photographs were of defendant, co-defendant Miller, or a third party. Defendant's counsel was given ample opportunity to cross-examine these witnesses and impugn their testimony. There is no evidence in the record that this photographic identification procedure was conducted in a prejudicial manner. As the courts so often state:

"We do not presume errors; we require the appellant to demonstrate it."

Sica v. United States, 325 F.2d 831 (9th Cir. 1963),  
at 836, cert. denied 375 U.S. 952.

The Government respectfully submits that this pretrial photographic display was not conducted improperly.



CONCLUSION

For the reasons stated above, the conviction should be affirmed.

Respectfully submitted,

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UNITED STATES OF AMERICA,

Appellee.

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APR 17 1968

*WM. B. LUCK CLERK*

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IN THE UNITED STATES COURT OF APPEALS  
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IN THE UNITED STATES COURT OF APPEALS  
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APPELLEE'S BRIEF

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JURISDICTION AND  
STATEMENT OF THE CASE

---

The appellant, Edmond Elijah Jensen was indicted along with John Smith, not an appellant herein, on June 28, 1967, by Federal Grand Jury for the Central District of California. 1/

Count Four of the indictment charges appellant Jensen and co-defendant John Smith unlawfully received, concealed and facilitated the concealment and transportation of 22.415 grams of heroin on February 28, 1967, in violation of Title 21, United States Code, Section 174. Count Five charges that on the same

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1/ C. T. 2; "C. T." refers to Clerk's Transcript of Proceedings.



date the defendants sold that amount of heroin to Agent William Jackson and an undercover assistant of the Federal Bureau of Narcotics, in violation of Title 21, United States Code, Section 174. Count Six charges that the defendants made such sale without obtaining a written order form from the purchasers, in violation of Title 26, United States Code, Section 4705(a) (C.T. 5-7).

Count Seven of the indictment charges that on or about March 8, 1967, appellant Jensen and defendant John Smith unlawfully received, concealed, and facilitated the concealment and transportation of 48.165 grams of heroin, in violation of Title 21, United States Code, Section 174. Count Eight charges that on the same date the defendants sold that amount of heroin to Agent William Jackson of the Federal Bureau of Narcotics, in violation of Title 21, United States Code, Section 174. Count Nine charges that the defendants made such sale without obtaining a written order form from the purchaser, in violation of Title 26, United States Code, Section 4705(a) (C.T. 8-10).

Counts One, Two, and Three of the indictment, which charged only defendant Smith, and dealt with violations of the Federal marihuana laws, were dismissed, on motion of the Government, prior to trial (C.T. 2-4, 16; R.T. 12-14).<sup>2/</sup>

Both defendants were arraigned on July 31, 1967, and both pleaded not guilty on August 21, 1967 (C.T. 11-12). On October 10, 1967, a bench trial was held as to both defendants,

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2/ "R.T." refers to Reporter's Transcript of Proceedings.



before the Honorable Peirson M. Hall, and the defendants were found guilty as charged in Counts Four, Five, Six, Seven, Eight and Nine of the indictment (C.T. 16).

On December 4, 1967, the appellant Jensen was convicted and sentenced to imprisonment for a period of five years as to Counts Four, Five, Seven, and Eight, all to run concurrent. A motion for acquittal as to Counts Six and Nine was granted at that time (C.T. 29).

Appellant filed Notice of Appeal on December 8, 1967 (C.T. 30).

The jurisdiction of the District Court is predicated on Title 21, United States Code, Section 174; Title 26, United States Code, Section 4705(a); and Title 18, United States Code, Sections 3231 and 3237.

This Court has jurisdiction under Sections 1291 and 1294, Title 28 of the United States Code.

#### STATUTES INVOLVED

Title 21, United States Code, Section 174, provides in pertinent part:

"Whoever fraudulently or knowingly . . . receives, conceals, buys, sells, or in any manner facilitates the transportation, concealment, or sale of any . . . narcotic drug after being imported or brought into the United States contrary to law . . .



shall be imprisoned not less than five or more than twenty years and, in addition, may be fined not more than \$20, 000 . . . .

"Whenever on trial for a violation of this section the defendant is shown to have or to have had possession of the narcotic drug, such possession shall be deemed sufficient evidence to authorize conviction unless the defendant explains the possession to the satisfaction of the jury."

Title 26, United States Code, Section 4705(a), provides:

"It shall be unlawful for any person to sell, barter, exchange, or give away narcotic drugs except in the pursuance of a written order of the person to whom such article is sold, bartered, exchanged, or given, on a form to be issued in blank for that purpose by the Secretary or his delegate."

#### STATEMENT OF FACTS

Agent William Jackson of the Federal Bureau of Narcotics met with an informant and the defendant, John Smith, at Smith's home on February 27, 1967 at 6:30 p. m. (R. T. 31). At that time, Agent Jackson told Smith that he wished to buy an ounce of good heroin (R. T. 32). Defendant Smith made a very short telephone call, hung up, and said, "Let's go." All three left in the informant's vehicle and proceeded, at Smith's direction to the inter-



section of New Avenue and Garvey Boulevard in South San Gabriel (R. T. 33).

There they parked near an ice cream stand, and Smith walked over to a telephone booth. Then he came back to the car and asked Agent Jackson for the money. Agent Jackson gave him \$360.00 and Smith walked around a corner, out of view (R. T. 33).

Approximately 20 minutes later, Smith returned, said that he had given the money to his man and that they would get delivery at the intersection of Hazard Street and City Terrace (R. T. 34).

They proceeded to that location and waited for an hour and a half, while nothing happened. Then, at Smith's direction, they drove back to the vicinity of New Avenue and Garvey Boulevard, and then to a house which Smith thought was his "man's" house but got no answer there, either (R. T. 34-35).

Smith then said to drive him home and not to worry about the money, that everything would be all right. He said that his "man" was a good friend of his and he was sure that delivery would be made the following morning (R. T. 53).

The next morning, the informant, Agent Jackson, and defendant Smith met at Smith's house at 9:00 a. m. (R. T. 36). Smith said he had talked to his man and everything was all right. They proceeded to Wabash and Evergreen Streets at Smith's direction, and Smith then got out and disappeared from view (R. T. 36).

About 10 minutes later, Smith was observed to get out of a light grey Hillman which had driven up and parked across the street, and was being driven by the defendant, Edmond Elijah



Jensen (R. T. 36).

The Hillman then drove from the area after Smith got out. Smith walked over to Jackson and handed him the heroin charged in Counts Four, Five, and Six of the indictment (R. T. 36 and 43).

Agent Jackson drove Smith home, met with the surveilling agents and searched the informant (R. T. 37).

Agent Jackson next called defendant Smith on March 8, 1967 and said he wished to buy two ounces of heroin and that he wanted to meet Smith's "man". Smith replied that this man, whose name was "Edmond" had been very good to Smith, and that Smith did not therefore want to introduce Jackson to him (R. T. 39).

Jackson then arranged to buy the two ounces in the same manner as in the previous transaction (R. T. 39).

That evening, Jackson drove over to Smith's house, not accompanied by the informant or anyone else (R. T. 39-40). Smith made a phone call and then left and drove again to New Avenue and Garvey Boulevard in South San Gabriel, where they again parked near the ice cream stand (R. T. 40).

Shortly after they arrived, Smith looked across the street and said, "There he is." In the parking lot of a Shell Station sat the same Hillman which had been seen on the previous occasion, and the defendant Jensen was standing on the passenger side by the front of the vehicle (R. T. 40).

Smith then asked Jackson for the money, and he was handed \$640.00. Whereupon, Smith then said, "I am not going to come back across the street after I get the stuff. You drive



over and pick me up." (R. T. 40).

Smith then left Agent Jackson's vehicle and joined defendant Jensen at the side of the Hillman, where they had a short conversation. They parted, Jensen re-entered the Hillman, Smith walked to the men's room of the Shell Station, stayed a very short while, and then walked to the corner of Garvey Boulevard and New Avenue (R. T. 40 and 43).

Agent Jackson drove his vehicle to that intersection and picked up defendant Smith who immediately handed him the heroin charged in Counts Seven, Eight, and Nine of the indictment (R. T. 41).

At the trial, Agent William Coonce testified that he was a surveilling agent at the time of the alleged transactions. On February 27, 1967, he observed defendant Smith make a telephone call near an ice cream store, and then get back into the informant's vehicle (R. T. 57).

Agent Coonce then observed a white, 1960 Falcon drive very slowly around the corner while its driver looked at the informant's vehicle and its occupants (R. T. 57).

Agent Coonce then took up a walking surveillance. He followed defendant Smith approximately a block and a half down the street, whereupon defendant Smith turned around and started walking toward Agent Coonce. At the same time, Agent Coonce again observed the 1960 Falcon now come toward Agent Coonce and turn in directly behind him. At this time, the driver of the Falcon was approximately five feet behind the agent (R. T. 57).



Agent Coonce observed the driver to be defendant Jensen (R. T. 58).

Agent Coonce was the surveilling agent again the following day. He was called by the informant who told him defendant Smith had explained to the informant that Smith had waited at the wrong intersection the night before for his source of supply to arrive, and that he had again talked to the source of supply, who was ready to deal that morning (R. T. 60).

On February 28, 1967, Agent Coonce, on surveillance, observed defendant Smith get out of the informant's and Agent Jackson's vehicle and proceed down Wabash Street. At this time, a gray Hillman appeared, and was being driven by the same person whom Agent Coonce saw driving the white Falcon the previous evening, namely defendant Jensen (R. T. 61).

Defendant Jensen picked up defendant Smith, turned around, and drove back to where the informant and Agent Jackson were waiting. Defendant Smith then got out of the car driven by defendant Jensen and re-entered the informant's vehicle (R. T. 61).

On the March 8, 1967 transaction, Agent Coonce instructed Agents Walker and Westrate to drive to a residence in Monterey Park, the address of which Agent Coonce had determined from the license plate registration of the Hillman he had observed on the February 28, 1967 transaction (R. T. 67).

At the same time as Agent Coonce was watching defendant Smith and Agent Jackson leave the residence of defendant Smith, the Hillman drove out of the driveway of the residence being



watched by Agents Walker and Westrate (R. T. 67-68).

Agents Coonce and Krueger followed defendant Smith to the intersection of New and Garvey, while Agents Walker and Westrate followed the Hillman to the same intersection. The Hillman then parked at the northwest corner, and defendant Jensen stood beside it (R. T. 68). Agent Coonce noted that it was the same defendant Jensen he had observed on the previous occasions in the white Falcon (R. T. 68).

Defendant Smith got out of the Government vehicle, crossed the street, and met with defendant Jensen where they held a short conversation (R. T. 68).

Defendant Smith then entered the restroom of the Shell Service Station where the Hillman was parked, and defendant Jensen left in the Hillman (R. T. 68).

The Hillman then proceeded back to the residence from which it had come, and the garage door closed (R. T. 68).

Meanwhile, defendant Smith and Agent Jackson were being followed back to defendant Smith's residence with the heroin charged in Counts Seven, Eight and Nine (R. T. 69).

On neither February 28, nor March 8, did defendant Smith or defendant Jensen request a written order form from Agent Jackson as required by law (R. T. 41).

At the trial, appellant Jensen produced no witnesses or testimony on his own behalf.



## ARGUMENT

### I

NO ERROR WAS COMMITTED BY CONSIDERING EVIDENCE THAT CO-DEFENDANT STATED, OUT OF PRESENCE OF APPELLANT, THAT APPELLANT WAS HIS "MAN", WHERE A COMMON SCHEME OR PLAN WAS PROVED.

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Appellant contends first that the trial judge "made the mistake of considering a mass of evidence, a great deal of which was admissible only against the co-defendant Smith." (Appellant's Opening Brief, page 9).

Apparently, appellant refers to several references in the testimony wherein the defendant Smith spoke of obtaining the heroin from his "man" (R. T. 34-36) whose name was "Edmond" (R. T. 39). When appellant arrived on the scene the co-defendant, out of his hearing, pointed to appellant and said, "There he is." (R. T. 40).

Though a continuing objection was sustained by the court as to those statements made out of the presence of appellant, assuming, for the sake of argument, that the court did consider this evidence against appellant, such consideration would not be improper. The testimony showed that immediately before producing the heroin on both occasions, the co-defendant Smith took the money from the narcotics agents and had a conversation with Jensen. On the second occasion, narcotics agents on surveillance followed Jensen from his own house to the meeting area, and then



back to his house again, without Jensen making any other stops or showing any other reason for the trip. These meetings and conversations between Smith and Jensen show that a plan existed between them, and permit the use of Smith's statements during the course of that plan against Jensen, despite the absence of a conspiracy charge in the indictment. As the court stated in United States v. Olweiss, 138 F.2d 798 (2d Cir., 1943), at page 800:

"The notion that the competency of the declarations of a confederate is confined to prosecutions for conspiracy has not the slightest basis; their admission does not depend upon the indictment, but is merely an incident of the general principle of agency that the acts of any agent, within the scope of his authority, are competent against his principal."

The test as to whether or not the statements and admissions of a co-defendant may be used against a defendant was laid down in Hitchman Coal and Coke Co. v. Mitchell, 245 U.S. 229 (1917), at page 249, where the court said:

"In order that the declarations and conduct of third parties may be admissible in such a case, it is necessary to show by independent evidence that there was a combination between them and defendants, but it is not necessary to show by independent evidence that the combination was criminal or otherwise unlawful." (emphasis added)



The case of Ong Way Jong v. United States, 245 F.2d 392

(9 Cir., 1957), is factually distinguishable. There, the court pointed out that, "It is conclusively shown that Wee had many sources of supply. It is firmly established in the evidence that on the sale by Wee of narcotics on January 23, 1956 (Appellant) Ong was not the supplier or 'connection' of Wee. More striking still is the fact that on the sale of narcotics by Wee on February 21, 1956, Ong was not the supplier or 'connection' of Wee. If there is anything which is proved by circumstantial evidence, it would seem to be that Ong was not the supplier of narcotics for the sale made by Wee on February 1, 1956." (page 395) In the instant case, on the other hand, Jensen was the only possible source of heroin supply, under the evidence, for defendant Smith. And, there being independent evidence of combination between Smith and Jensen on both occasions of sale, the statements of Smith made during the course of that combination would be admissible against Jensen.

Lutwak v. United States, 344 U.S. 604 (1953).

## II

CIRCUMSTANTIAL EVIDENCE IS SUFFICIENT TO CONVICT DEFENDANT JENSEN, EVEN WITHOUT SMITH'S DECLARATIONS, WHERE THE GOVERNMENT DID NOT SEARCH THE CO-DEFENDANT SMITH.

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In the above case where defendant Smith had to go somewhere else for the heroin and never was able to produce it without first meeting with defendant Jensen; and where defendant Jensen



was seen driving around in the 1960 Falcon on February 27, looking the situation over, and then appearing in a Hillman on February 28 and briefly meeting with defendant Smith just before Smith was able to produce the heroin, there is sufficient evidence to support the conclusion that defendant Jensen was defendant Smith's source of supply, even without using the evidence that Smith pointed across the street to Jensen and said, "There he is." And even more incriminating evidence exists on the subsequent March 8 transaction, when two surveilling agents staked out defendant Jensen's residence, saw him leave in the Hillman, followed him to the meeting with defendant Jensen, and then followed him right back to his garage, while defendant Smith was delivering the heroin to the other agents. What other reasonable explanation was offered for this excursion?

Circumstantial evidence, is of course, competent for conviction under this statute. See Rodella v. United States, 286 F.2d 306, 312 (9th Cir., 1960), and the cases cited therein.

Appellant cites People v. Ollado, 246 Cal. App. 2d 608 (1966); Dear Check Quong v. United States, 160 F.2d 251 (D.C. Cir. 1947); Panci v. United States, 256 F.2d 308 (5th Cir., 1958); United States v. Rossi, 219 F.2d 612 (2d Cir., 1955); People v. Barnett, 118 Cal. App. 2d 336 (1953); and Gutierrez v. United States, 314 F.2d 334 (5th Cir., 1963), as standing for the proposition that unless Smith was searched by the agent, prior to leaving the automobile, a conviction against Jensen ought not to stand. These cases deal with informant purchases, not purchases by defendants who are



attempting to sell narcotics and are not out to "make a case" on another individual. To require that a narcotics agent, working undercover, search a defendant before the defendant leaves to pick up the heroin he's been paid for, would be contrary to common sense.

### CONCLUSION

A review of the entire record indicates no error prejudicial to the rights of appellant and, accordingly, the judgment below should be affirmed.

Respectfully submitted,

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WILLIAM J. GARGARO, JR.  
Assistant U. S. Attorney

Attorneys for Appellee  
United States of America



CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ William J. Gargaro, Jr.

WILLIAM J. GARGARO, JR.



**United States Court of Appeals  
FOR THE NINTH CIRCUIT**

JACK RAY CULBERTSON,

Petitioner and Appellant,

vs.

STATE OF CALIFORNIA,  
et al.,

Respondents and Appellees.

On Appeal From the United States District Court  
For the Southern District of California

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APPELLANT'S OPENING BRIEF

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FILED

FEB 20 1968

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FEB 27 1968



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UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

JACK RAY CULBERTSON,

Petitioner and Appellant,

vs.

STATE OF CALIFORNIA,  
et al. ,

Respondents and Appellees.

---

APPELLANT'S OPENING BRIEF

---

STATEMENT OF THE CASE

Petitioner was convicted in the Municipal Court of the San Diego Judicial District of exhibiting obscene films in violation of Section 311.2 of the Penal Code of California on August 16, 1965 after a trial before a jury. Prior to the trial, the court viewed the films and held them to be obscene as a matter of law.

In November, 1965, sentence was suspended and petitioner was granted probation of one year and said period has expired.

Petitioner appealed to the Appellate Department of the Superior Court of the San Diego County and his conviction was affirmed. Certification to the Court of Appeal of the Fourth Appellate District was denied. In June, 1966, while still on probation, petitioner filed a Writ of Habeas Corpus in the United States District Court (# 3585) Southern District of California, Southern Division alleging that he had

suffered an unlawful search and seizure in violation of the Fourth Amendment of the Constitution of the United States and that the material seized was constitutionally protected and that he was denied freedom of speech and press under the First Amendment of the Constitution of the United States and further that defendant suffered self incrimination and was denied due process of law. On September 14, 1966 said United States District Court dismissed the application for a Writ of Habeas Corpus. Petitioner did not appeal from this order.

On October 3, 1967, petitioner filed a Writ of Error Coram Nobis alleging the above facts and that until said date petitioner was unaware that the United States District Court did not view the exhibits submitted in behalf of petitioner at the time the Writ of Habeas Corpus was denied and that the order dismissing said Writ was therefore based on insufficient evidence and further that said United States District Court did not grant petitioner a hearing and that petitioner was entitled to a Writ of Coram Nobis for the reasons that an error of law had taken place and that the films were not obscene either at the time of his conviction in the Municipal Court of the San Diego Judicial District, citing Jacobellis v. Ohio, 378 U.S. 184; and Roth v. United States, 354 U.S. 476 or under the later decision of the United States Supreme Court in Redrup v. New York, 386 U.S. 767 and companion cases (1967). Petitioner also alleged that the result of said conviction persists to this date in that subsequent convictions under the California Penal Code will carry a heavier penalty as a felony and his civil rights as a citizen of the United States would be lost. Petitioner also pointed out that a Writ of Error Coram Nobis will not lie in the State of California if he seeks redress by reason of an error of law rather than a mistake of fact.

On November 6, 1967, the City Attorney of the City of San Diego filed a Notice of Motion to Dismiss said Writ of Error Coram Nobis upon the ground that the petition does not invoke the jurisdiction of the United States District Court alleging that said Writ could not be used as a substitute for a Writ of Habeas Corpus or as a collateral writ of error between State and Federal jurisdictions. On November 21, 1967 said District Court dismissed the petition for a Writ upon the ground that petitioner was alleging error in a civil action and that coram nobis was not available for such a purpose under Federal Rule 60(b) and also that the Writ could not be treated as one for habeas corpus because petitioner was no longer in custody and upon the further ground that petitioner was seeking to have the court apply concepts of obscenity which were not in existence at the time of his conviction and give retrospective effect to the Redrup decision. Petitioner filed a Notice of Appeal and the District Court granted a Certificate of Probable Cause which is on file in this appeal.

#### SPECIFICATION OF ERRORS

1. The court erred in dismissing the petition for a Writ for lack of jurisdiction.
2. The Court erred in holding that the Writ is not available under Rule 60(b) of the Federal Rules of Procedure.
3. The Court erred in holding that the material was not constitutionally protected under the decisions in effect at the time the Writ of Habeas Corpus was filed.
4. The Court erred in failing to apply the concepts of obscenity as set forth in Redrup v. New York.
5. The Court erred in holding that a Writ of Habeas Corpus is not available because petitioner is not in custody.

## ARGUMENT

### I

#### THE WRIT OF ERROR CORAM NOBIS IS AVAILABLE TO PETITIONER EVEN THOUGH IT IS FILED IN A CIVIL ACTION BECAUSE PETITIONER HAS SUFFERED A CRIMINAL CONVICTION.

In the recent case of In re Gault, 387 U.S. 1, the United States Supreme Court has extended constitutional guarantees to proceedings in juvenile cases which heretofore have been considered "civil" actions although the proceedings grew out of criminal offenses committed by minors. The fiction that these proceedings were not criminal in nature was formulated for the purpose of protecting minors from suffering liabilities by reason of a criminal conviction. The Court states in the Gault case:

"It would be entirely unrealistic to carve out of the Fifth Amendment all statements by juveniles on the ground that these cannot lead to 'criminal' involvement. In the first place, juvenile proceedings to determine 'delinquency' which may lead to commitment to a State Institution must be regarded as 'criminal' for purposes of the privilege against self-incrimination. To hold otherwise would be to disregard substance because of the feeble enticement of the 'civil' label-of-convenience which has been attached to juvenile proceedings. . . . It is incarceration against one's will whether it is called 'criminal' or 'civil'. And our Constitution guarantees that no person shall be 'compelled' to be a witness against himself when he is threatened with deprivation of his liberty - a command which this court

has broadly applied and generously implemented in accordance with the teaching of the history of the privilege and its great office in mankind's battle for freedom." (Citing Miranda v. Arizona, 384 U. S. 436 and other cases.)

In line with the reasoning of the United States Supreme Court in Gault and looking at the substance rather than the form, it is obvious that the filing of a Writ of Error Coram Nobis in the case at bench involves criminal proceedings and especially, as in this case, where petitioner has suffered criminal conviction. It would be contrary to the basic tendencies of the Federal Courts to extend relief in criminal cases if so important a Writ could be dismissed on the minimal ground that it is a "civil" proceeding. It has been held that rule 60(b) does not apply to criminal proceedings and petitioner alleges this exception to rule 60(b) extends to cases which are criminal in nature, Sanchez v. Tapia v. U. S., 227 F. Supp. 35, affirmed 338 F. 2d 416, certiorari denied 380 U. S. 957; U. S. v. Marcello, 210 F. Supp. 892, affirmed 328 F. 2d 961, certiorari denied 377 U. S. 992.

With regard to Habeas Corpus, the fact that petitioner is no longer in custody is immaterial since the result of his conviction persists and the Federal Court will not suffer him to be without a remedy if, as in the case at bench, he has been denied fundamental constitutional rights for which he is entitled to redress. Morgan v. United States, 346 U. S. 562; Sanders v. United States, 373 U. S. 1.

## II

PETITIONER IS ENTITLED TO RELIEF WHETHER BY WRIT OF CORAM NOBIS OR HABEAS CORPUS.

In Fay v. Noia, 372 U.S. 391, petitioner and two other persons were convicted of murder. The petitioner did not appeal as his co-defendants did. He applied to the State court for a coram nobis review of his conviction but this was denied because of his failure to appeal. He then filed a Writ of Habeas Corpus in a United States District Court which was denied. The Court states that after State courts had dismissed Federal questions on the merits against the petitioner, he could apply to the Federal Court for habeas corpus and relitigate the question and that conventional notions of finality in criminal litigation cannot be permitted to defeat the manifest Federal policy that constitutional rights of personal liberty shall not be denied without the fullest opportunity for plenary federal judicial review. The court further held that Federal Court jurisdiction in a habeas corpus proceeding is conferred by the allegation of an unconstitutional restraint, and it is not defeated by anything that may occur in the State proceeding and that forfeiture of remedy does not legitimize the unconstitutional conduct by which his conviction was procured.

Appellant, in the case at bench, alleges that he was denied fundamental constitutional rights which cannot be defeated by his failure to appeal from the denial of the Writ of Habeas Corpus in the Court below.

In Lark v. U.S. (1965) 251 F. Supp. 471, petitioner sought to set aside a 1925 federal conviction. The court and the Government conceded that the court had jurisdiction despite failure to appeal or bring writs over this extended period of time.

CONCLUSION

In view of the foregoing, appellant prays that the order of the United States District Court dismissing the Writ of Error Coram Nobis be reversed.

Respectfully submitted,

HARRY ELLMAN and  
MELVYN B. STEIN

By /s/ HARRY ELLMAN

Attorneys for Appellant.

CERTIFICATION

I certify that in connection with the preparation of this Brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit and that in my opinion the foregoing Brief is in full compliance with those rules.

/s/ HARRY ELLMAN



**United States Court of Appeals  
FOR THE NINTH CIRCUIT**

JACK RAY CULBERTSON,

Petitioner and Appellant,

vs.

STATE OF CALIFORNIA, et al.,

Respondents and Appellees.

On Appeal From the United States District Court  
For the Southern District of California

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APPELLANT'S REPLY BRIEF

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**FILED**

APR 1 1958

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UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

JACK RAY CULBERTSON,

Petitioner and Appellant,

vs.

STATE OF CALIFORNIA, et al.,

Respondents and Appellees.

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APPELLANT'S REPLY BRIEF

---

STATEMENT OF THE CASE

The facts on this appeal are set forth in Appellant's Opening Brief. Appellant replies to the points made by respondents with respect to the dismissal of the Writ in the Court below upon the ground that the present Writ is a "civil" proceeding and is therefore barred by Rule 60 (b) of the Code of Federal Procedure and because Appellant was not in State custody at the time the present Writ was filed. Respondents also contend that the decision of the United States Supreme Court in Redrup v. New York, 386 U. S. 767 is not retroactive.

Appellant previously filed a Writ of Habeas Corpus at the time he was serving a probationary term, in the case at bench.

ARGUMENT

## I

THE DISTRICT COURT ERRED IN DISMISSING THE PETITION ON THE GROUNDS THAT THE WRIT WAS FILED IN A CIVIL PROCEEDING OR BECAUSE PETITIONER WAS NO LONGER IN STATE CUSTODY

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Respondents contend that the case of United States v. Morgan (1954) 346 U. S. 502, 98 L. Ed. 248 is authority for the principal that a Writ of Error Coram Nobis is not a proper device for a review of a State conviction by the Federal Courts. In that case petitioner filed a Coram Nobis Writ in the Federal Court after he was convicted by a New York court on a State charge. The sentence in the State court was made longer as a result of his previous conviction on a federal charge. At the time of the filing of the Writ of Coram Nobis he had served his sentence on the federal offense. He was, however, still incarcerated in a State prison. The United States District Court had dismissed the Writ on the ground that it had no jurisdiction as applicant was no longer in custody under the Federal sentence.

In the case at bench, appellant had filed a petition for a Writ of Habeas Corpus within his probationary period.

Respondents cite the case of Rivenburgh v. Utah (1962) 299 F. 2d 842, 843, in support of their claim that Coram Nobis cannot be used to support a collateral attack on a State judgment. Appellant is not doing this in the case at bench, Further the Rivenburgh case, supra, dealt with a claim that applicant should be granted a new trial because of newly discovered evidence. In the case at bench, no such contention is made, but rather, that the United States District Court erred in dismissing the Writ of Habeas Corpus.

Respondents cite the case of Parker v. Ellis (1960) 362 U. S. 574, 4 L. Ed. 2d 963 in which the United States Supreme Court dismissed a Writ of Certiorari because petitioner had been released from State Imprisonment before the case could be heard. In the case at bench, however, appellant is not attacking State proceedings but rather the validity of the denial of the Writ of Habeas Corpus which was filed at a time when he was still in custody. Moreover appellant is subject to additional punishment as a recidivist under the provisions of the Penal Code of California, making subsequent convictions for the same offense a felony. Under the Morgan decision, although petitioner's probationary term has expired, the Court has jurisdiction where the results of a conviction may persist and subsequent convictions carry heavier penalties and where his civil rights, as in the case of a convicted felon, may be affected. Fiswick v. United States, 329 U. S. 211.

The real issue on this appeal is whether appellant in the case at bench still has a remedy even though he did not appeal from the previous denial of the Writ of Habeas Corpus.

Appellant is frank to admit that he seeks appellate review by a new Writ although his time to appeal has expired because he has been denied constitutional rights of fundamental character and technical objections should not be permitted to deny him these rights. Fay v. Noia, 372 U. S. 391

## II

THE WRIT OF HABEAS CORPUS SHOULD HAVE BEEN GRANTED EITHER ON THE LAW IN EXISTENCE AT THE TIME THE ORIGINAL WRIT WAS FILED OR UNDER REDRUP V. NEW YORK

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Respondents go to great pains to argue whether the case of Redrup v. New York, 386 U. S. 767 should be applied retrospectively. Appellant contends that this is immaterial since the Writ should have been granted on the authority of Roth v. United States, 354 U. S. 476 and Jacobellis v. Ohio, 378 U. S. 184.

In further answer to the contention of respondents, the present appeal is not moot because the result of appellant's conviction persists as pointed out in the previous paragraph.

In none of the cases cited by respondents on page 12 of their brief is there a Statute which makes a repetition of the offense subject to the penalty of a felony with resultant loss of civil rights.

CONCLUSION

In view of the foregoing, appellant prays that the order of the United States District Court dismissing the Writ of Error Coram Nobis be reversed.

Respectfully submitted,

HARRY ELLMAN and  
MELVYN B. STEIN

By: /s/ HARRY ELLMAN

Attorneys for Petitioner and Appellant.

CERTIFICATION

I certify that in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit and that in my opinion the foregoing brief is in full compliance with those rules.

/s/ HARRY ELLMAN



**United States Court of Appeals  
FOR THE NINTH CIRCUIT**

JACK RAY CULBERTSON, )  
Petitioner and Appellant, )  
vs. ) No. 22555  
STATE OF CALIFORNIA, et al., )  
Respondents and Appellees. )  
\_\_\_\_\_ ) RESPONDENT'S BRIEF

On Appeal From the United States District Court  
For the Southern District of California

**BRIEF OF THE CITY OF SAN DIEGO**

**AS RESPONDENT**

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**FILED**

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MAR 20 1966

WM. B. LUCK CLERK



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UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

JACK RAY CULBERTSON, )  
                          )  
Petitioner and Appellant, )  
                          )  
                          ) No. 22555  
vs.                     )  
                          ) RESPONDENT'S BRIEF  
STATE OF CALIFORNIA and )  
CHARLES T. G. ROGERS, )  
                          )  
Respondents and Appellees. )  
                          )  
-----)



## STATEMENT OF THE FACTS

Appellant owned and operated the "E Street Newsstand" located at 429 "E" Street in San Diego, California. He sold periodicals, cigarettes, sundries and photographs and also exhibited so-called "girlie" films on coin operated projectors located in small, individual booths within the store. On March 16, 1965, appellant was arrested and charged with violating California Penal Code Section 311.2<sup>1</sup> for the exhibition of four reels of film on the above-described projectors.

## STATEMENT OF THE PROCEEDINGS BELOW

On March 19, 1965, appellant was formally arraigned and charged with a violation of Section 311.2, at which time he entered a plea of not guilty. The case

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### 1. "Section 311. Definitions

As used in this chapter:

(a) 'Obscene' means that to the average person, applying contemporary standards, the predominant appeal of the matter, taken as a whole, is to purient interest, i.e., a shameful or morbid interest in nudity, sex, or excretion, which goes substantially beyond customary limits of candor in description or representation of such matters and is matter which is utterly without redeeming social importance.

(b) 'Matter' means any book, magazine, newspaper, or other printed or written material or any other picture, drawing, photograph, motion picture, or other pictorial representation or any statue or other figure, or any recording, transcription or mechanical, chemical or electrical reproduction or any other articles, equipment, machines or materials.

(c) 'Person' means any individual, partnership, firm, association, corporation, or other legal entity.

(d) 'Distribute' means to transfer possession of, whether with or without consideration.

(e) 'Knowingly' means having knowledge that the matter is obscene. (Added Stats. 1961, c. 2147, p. 4427, § 5.)

"311.2 Sending or bringing into state for sale or distribution; printing, exhibiting, distributing or possessing within state

Every person who knowingly: sends or causes to be sent, or brings or causes to be brought, into this State for sale or distribution, or in this State prepares, publishes, prints, exhibits, distributes, or offers to distribute, or has in his possession with intent to distribute or to exhibit or offer to distribute, any obscene matter is guilty of a misdemeanor. (Added Stats. 1961, c. 2147, p. 4428, § 5.)"

2.

came to trial on August 10, 1965. The Honorable Earl B. Gilliam, Judge, sitting without a jury, made the initial determination that the films were obscene as a matter of law. Appellant was subsequently tried and found guilty by a jury. On November 8, 1965, appellant's sentence was suspended and probation for one year was granted. Appellant filed a Notice of Appeal on November 8, 1965, and duly pursued his appellate remedy before the Appellate Department of the Superior Court of San Diego County. Appellant's conviction was affirmed by the Appellate Department on May 25, 1966.<sup>2</sup> The transfer on certification to the District Court of Appeal of the State of California, Fourth Appellate District, was denied on June 13, 1966. On June 27, 1966, petitioner filed an application for a writ of habeas corpus in the United States District Court for the Southern Division of California, which application was denied on September 14, 1966. Petitioner did not appeal. The one-year probationary period expired on November 8, 1966. On October 3, 1967, petitioner filed a writ of error coram nobis with the United States District Court for the Southern Division of California. On November 6, 1967, respondent filed a Notice of Motion, Motion to Dismiss, and Points and Authorities supporting said Motion, in opposition to petitioner's application for said writ. On November 22, 1967, the district court dismissed the petition for the writ of error coram nobis. Appellant appeals from the order dismissing the writ.

## SPECIFICATION OF ISSUES

Three basic issues are presented to this court by petitioner's Specification of Errors.<sup>3</sup>

1. Did the district court err by dismissing the petition for a writ, whether considered as a writ of error coram nobis or a writ of habeas corpus?
2. Did the district court err by refusing to review the habeas corpus proceeding of June 27, 1966, pursuant to appellant's application for a writ of error coram nobis?
3. Did the district court err by refusing to apply retrospectively the rule of Redrup v. New York, 386 U.S. 767 [18 L. Ed. 2d 515] and the June 12, 1967 decisions following Redrup?

## ARGUMENT

### I

#### THE DISTRICT COURT DID NOT ERR BY DISMISSING THE PETITION FOR A WRIT, WHETHER THE WRIT WAS FOR ERROR CORAM NOBIS OR HABEAS CORPUS

Petitioner's argument that the district court committed error is based on two different conceptual applications of the writ of error coram nobis, both of which are mistaken.

First, petitioner urges that coram nobis is a proper means of reviewing the habeas corpus proceeding of June 27, 1966, in the district court.<sup>4</sup>

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3. Page 3 of petitioner's brief.

4. See Petition for Writ of Error Coram Nobis, 67-226-K, filed October 31, 1967 in the District Court, p. 3, Section VIII, pp. 3-4, Section IX, p. 4  
(continued on following page)

Second, petitioner argues that either coram nobis or habeas corpus will afford him a vehicle for a new and independent review of the original conviction in the state municipal court by the district court.<sup>5</sup>

An evaluation of petitioner's second contention will lay the foundation for dealing with his first argument.

#### Coram Nobis

The writ of error coram nobis is not a proper device for the review of a state conviction by the United States District Court. United States v. Morgan (1954) 346 U.S. 502 [98 L. Ed. 248]. The Morgan case teaches us that in regard to federal prisoners, jurisdiction may be conferred by the All Writs Section of the Judicial Code, 28 U.S.C. § 1651(a)<sup>6</sup> upon the federal court that imposed the sentence even though the federal prisoner may have served the sentence. Coram nobis may not, however, be used as a collateral writ of error between state and federal

4. (continued from preceding page)

Section XI (1) and (4); Petitioner's Points and Authorities in Reply, 67-226-K, filed November 17, 1967 in the District Court, p. 1, lines 3-5, lines 16-21; Appellant's Opening Brief, No. 22555, filed with this Court, p. 3, Specification of Errors numbered as 1, 2 and 3.

5. See Petition for Writ of Error Coram Nobis, 67-226-K, filed October 31, 1967 in the District Court, pp. 4-5, Section XI (a) (3) (5) and (6); Petitioner's Points and Authorities in Reply, 67-226-K, filed November 17, 1967 in the District Court, p. 1, lines 26-29, p. 3, lines 7-19; Appellant's Opening Brief, No. 22555, filed with this Court, Specification of Errors numbered as 1, 4 and 5.

6. 28 U.S.C. § 1651(a) provides: "The Supreme Court and all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law."

jurisdictions.<sup>7</sup> The United States Court of Appeals, Tenth Circuit, faced the issue in Rivenburgh v. Utah (1962) 299 F.2d 842, 843:

"[1-3] Coram nobis is a remedy recognized in some state judicial systems and as such may premise an ultimate review of state action by way of certiorari to the Supreme Court of the United States. Hamilton v. Alabama, 368 U.S. 52, 82 S.Ct. 157, 7 L.Ed.2d 114. And the writ is sometimes broadly recognized as available in matters strictly confined within the federal judicial system. Dotson v. United States, 10 Cir., 287 F.2d 868; United States v. Morgan, 346 U.S. 502, 74 S.Ct. 247, 98 L.Ed. 248. But the use of the writ is limited by tradition and rule, Fed. rules Civ. Proc., Rule 60(b), 28 U.S.C.A., and cannot be used as a substitute for habeas corpus or as a collateral writ of error between state and federal jurisdictions. The essence of petitioner's claim is that he should be granted a new trial because of newly discovered evidence. We are in complete accord with the trial's [sic] court order that the petition sets out no federal basis or claim for relief cognizable in the federal court.

The motion to dismiss the appeal is granted and the appeal is dismissed."

The citation by appellant of the Morgan case does nothing to sustain his

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7. This court has recognized the principle as set forth in Morgan. See Madigan v. Wells, (9th Circ. 1955) 224 F.2d 577, footnote 2, Cert. den. 351 U.S. 911 [100 L.Ed. 1446] and In re Lempia (9th Circ. 1956) 247 F.2d 240, Cert. den. 352 U.S. 931 [1 L.Ed.2d 166]. A discussion of the rule is carried in 49 C.J.S. 313(b) (1947).

jurisdictional argument. In Morgan the petitioner filed his application for a writ of error coram nobis in the federal district court where he was first tried and convicted. Here, appellant seeks to use coram nobis as a means of collateral review of his original conviction in the state court. Clearly, this is not the purpose of coram nobis. The district court has no jurisdiction to entertain such an application and the petition filed on these grounds was properly denied. The denial should be affirmed.

#### Coram Nobis Considered As Habeas Corpus

The application by appellant herein for a writ of error coram nobis, whether considered as coram nobis or as habeas corpus, fails to confer jurisdiction on the district court for another reason.

In the case of Parker v. Ellis (1960) 362 U.S. 574 [4 L. Ed. 2d 963] the United States Supreme Court ruled that, where petitioner had made application in federal court for a writ of habeas corpus seeking a review of a state conviction and where, prior to the hearing on habeas corpus, petitioner had been released from state prison and was not placed on parole, the case had become moot. The court determined that it was without jurisdiction to deal with the merits of petitioner's claim. It refused to proceed to adjudication where there was no subject matter on which the judgment of the court could operate.<sup>8</sup>

This rule of law has been recognized and followed by the United States Court of Appeals, Ninth Circuit. In Bonnie v. Gladden (9th Circ. 1967) 377 F. 2d 555, while petitioner's appeal of the denial of a petition for writ of habeas

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8. At page 575 of the decision.

corpus was pending, his sentence was completed and he was discharged from confinement without parole. Under these circumstances the court ruled:

"In light of this development we are without power to deal with the merits of Bonnie's claim under the interpretation of the 'in custody' requirement of 28 U.S.C. 2241(c) (1) (1964) adopted in Parker v. Ellis, 362 U.S. 574, 80 S.Ct. 909, 4 L.Ed.2d 963 (1963).

"The case must therefore be remanded to the district court with instructions to vacate the order appealed from and dismiss the application for habeas corpus."<sup>9</sup>

The principle as described and followed in Bonnie was also held to be controlling in Benson v. State Board of Parole and Probation (9th Circ. 1967) 384 F.2d 238. In the Benson case petitioner's declaratory relief action was dismissed as moot when his state prison sentence had expired. Petitioner argued that he continued to suffer the consequences of the state conviction for forgery regardless of the expiration of his sentence. He asserted that as a result of his conviction he lost his license as a public accountant and insurance agent, was disqualified as a juror, and was burdened with "liability to future enhanced punishment."<sup>10</sup>

Petitioner's arguments notwithstanding, the court ruled that it was without power to consider the merits of the state prisoner's case where he had completed his sentence. It found petitioner's application of the Morgan principle to be improper. In referring to Morgan and comparing it to Parker v. Ellis, the court determined that "there is no suggestion that the writ of coram nobis would

9. At page 555.

10. At page 239. The last assertion is taken to mean that in the event of subsequent convictions, petitioner could expect harsher punishment due to his earlier conviction.

be available to a state prisoner whose custody has terminated." <sup>11</sup>

Further, it is settled law in the Ninth District that the All Writs Statute does not confer jurisdiction upon the district court in cases where the issues are rendered moot by reason of the unconditional release of the prisoner and appellant. The court in Benson followed its earlier ruling in Stafford v. Superior Court of California (9th Circ. 1959) 272 F.2d 407, and determined that the All Writs Statute may be invoked by the district court only in the aid of jurisdiction which it already has. The Statute may not be used to confer jurisdiction where none otherwise exists. <sup>12</sup>

The conclusion is inescapable that the court below correctly ruled that it was without jurisdiction to hear appellant's case on its merits. Further, appellant has cited no authority which would authorize this court to rule otherwise. Those cases relied on by appellant are either distinguishable from, or entirely inapplicable to, the case before the court. <sup>13</sup>

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11. At page 239. For a similar conclusion see Cole v. United States (10th Circ. 1963) 311 F.2d 492.

12. At pages 239-240.

13. Those cases cited by appellant that are not discussed in the body of respondent's brief are distinguished here. In re Gault, 387 U.S. 1, contained facts so completely unrelated to those in this case that its citation is irrelevant. To generalize, Gault ruled that due process requirements must be observed in juvenile court proceedings. There was nothing in Gault to suggest that the district court in this case had jurisdiction to entertain a petition for a writ of error coram nobis. Miranda v. Arizona, 384 U.S. 436, has no application to this case whatsoever. Respondent was somewhat perplexed by appellant's citation of Sanchez Tapia v. U.S., 227 F. Supp. 35, affirmed 338 F.2d 961, Cert. den. 380 U.S. 957. The case sustains respondent's position. The appellant in Sanchez was originally convicted and sentenced in the U.S. District Court for the District of Puerto Rico. Appellant then brought

The district court properly denied the petition filed by appellant on the above grounds and the denial should be affirmed.

## II

### **THE DISTRICT COURT DID NOT ERR BY REFUSING TO REVIEW THE HABEAS CORPUS PROCEEDING OF JUNE 27, 1966 PURSUANT TO APPELLANT'S APPLICATION FOR A WRIT OF ERROR CORAM NOBIS**

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As was explained above, the essence of appellant's argument contemplates a review of the state court conviction. In an effort, however, to avoid the inevitable problems created by the impropriety of such an action, appellant also asserts that coram nobis was sought in the district court as a review by that court of its own habeas corpus proceeding of June, 1966. It is noteworthy that no authority is cited by appellant to indicate that the court below had jurisdiction to entertain a coram nobis petition for this purpose.<sup>14</sup>

The fact is that appellant seeks to warp the device of coram nobis to suit his

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13. (continued from preceding page)

a petition for coram nobis in the U.S. District Court for the Southern District of New York. The District Court in New York granted the government's motion to dismiss the application concluding that it had no jurisdiction to act. It ruled that the appellant's remedy was in the trial court in which appellant was tried, convicted and sentenced. Again, the citation by appellant of U.S. v. Marcello, 210 F. Supp. 892, affirmed 328 F.2d 961, Cert. den. 377 U.S. 992, sustains respondent's position. Petitioner in Marcello correctly applied for relief in the trial court in which he originally suffered a conviction. The same facts were evident in Lark v. U.S., 251 F. Supp. 471. Appellant herein cited Sanders v. U.S., 373 U.S. 1, to sustain his argument that "the fact that petitioner is no longer in custody is immaterial since the result of his conviction persists." The defendant in Sanders was in custody at the time he pursued his application for a writ of habeas corpus, thus, the case does not sustain appellant's argument. In Fay v. Noia, 372 U.S. 391, similar facts existed; petitioner was in custody while he sought a writ of habeas corpus.

14. Appellant's cases are distinguished in note 13 above.

own purposes. The writ was never meant to confer jurisdiction under these circumstances. This most liberal application of coram nobis makes it clear that the writ enables the trial court to review its own trial proceedings and judgment.<sup>15</sup> Coram nobis is not a proper means of reviewing the denial of a petition for habeas corpus; this is now made clear by statute.<sup>16</sup> A careful reading of Morgan, the case upon which appellant so heavily relies, shows the correctness of the application of Federal Rule 60(b) by the judge in the district court proceedings. The Supreme Court restated the established rule that habeas corpus affords relief in a separate case and record, the beginning of an entirely separate civil proceeding.<sup>17</sup> Any review of a habeas corpus proceeding is a review of a civil proceeding and no amount of rationalization by appellant can change the law. Thus, the district court was correct in its conclusion that it lacked jurisdiction. Rule 60(b) has abolished coram nobis as a writ for the review of civil proceedings.

Let us assume, however, that the court below could have found jurisdiction to consider appellant's petition. The court would still have been compelled to deny the application because appellant sought to remedy an alleged wrong that coram nobis could not reach. Coram nobis lies for an error of fact in existence at the time of trial though not apparent on the record, and which, if known by the trial

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15. U.S. v. Morgan at pages 505, 507, 509.

16. Fed. Rule 60(b) in applicable part reads: "Writs of coram nobis, coram vobis, audita querela, and bills of review and bills in the nature of a bill of review, are abolished, and the procedure for obtaining any relief from judgment shall be by motion as prescribed in these rules or by an independent action."

court would have prevented the rendition of judgment.<sup>18</sup> Appellant, by his own acknowledgment,<sup>19</sup> seeks redress for an alleged error of law. Coram nobis does not afford such redress.

Again, the district court properly denied appellant's petition filed on the above grounds and the denial should be affirmed.

### III

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#### THE DISTRICT COURT DID NOT ERR BY REFUSING TO APPLY RETROSPECTIVELY THE REDRUP CASE AND THE JUNE 12, 1967 DECISIONS FOLLOWING THAT CASE

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Appellant contends that on October 31, 1967, the court below should have applied the principles set forth in the May 8, 1967 case of Redrup v. New York, 386 U.S. 767 [18 L. Ed. 2d 515], the principle of which was followed in thirteen of the sixteen obscenity cases decided by the Supreme Court on June 12, 1967. By November 8, 1966, the petitioner had completed the term of his probation and his sentence was served. Stated differently, appellant completed the serving of his sentence nearly twelve months prior to the filing of the application for a writ of error coram nobis in the court below. To comply with appellant's contention the district court would have had to apply retrospectively the new obscenity cases to either the state conviction of August 10, 1965 or to the habeas corpus proceeding of June 27, 1966.

Appellant relies upon the thirteen June 12, 1967 Supreme Court decisions

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18. U.S. v. Morgan at pages 507, 509. For a general discussion of the rule see 49 C.J.S. § 313(c) (d).

19. See the last line of page 2 of Appellant's Opening Brief.

in which convictions were reversed, but he ignores two of the three remaining obscenity cases decided by the Supreme Court on the same day, Jacobs v. New York, 388 U.S. 431 [18 L. Ed. 2d 1294] and Tannenbaum v. New York, 388 U.S. 439 [18 L. Ed. 2d 1300]. In both cases motions to dismiss were granted and the appeals were dismissed as moot. In each case suspended sentences had been levied against the appellants. The applicable state law recited that the maximum time during which the appellants could have had their sentences revoked and replaced by prison terms was one year from the date of sentencing. More than one year had elapsed while the respective appeals were pending, thus, the appellants had, in effect, served their sentences and their cases were ruled moot.<sup>20</sup>

It is clear the Supreme Court does not intend that newly defined concepts of obscenity be applied retrospectively when a case has been rendered moot by reason of the completion of the sentence. This was held to be the law even where the appellate process in the two cases cited above was begun prior to the expiration of the period within which the appellants stood in jeopardy, whether by reason of confinement, fine, suspended sentence or parole. Certainly the same principle is applicable to the process of collateral attack upon a conviction, especially when the institution of that attack was subsequent to the case having

20. Jacobs v. New York at page 432. It is interesting to note the positions taken by the respective justices. In the Jacobs case, the motion to dismiss the case as moot was granted by a five-justice majority. Justice Brennan would have affirmed the conviction, Justice Fortas would have reversed the conviction, Chief Justice Warren wanted to face the issue of obscenity and disagreed with the application of the mootness doctrine, and Justice Douglas wanted to see the mootness issue briefed and argued. In the Tannenbaum case Justice Fortas joined the majority on granting the motion to dismiss for mootness, Justice Brennan would have reversed the conviction and the Chief Justice and Justice Douglas stood by their dissenting opinions in Jacobs.

become moot.

This resolution by the Supreme Court of the problem of retrospective application of new obscenity decisions to mooted cases precludes the need for a discussion of the general principles of retrospective application<sup>21</sup> which, in themselves, would preclude the court below from applying the Redrup and June 12, 1967 decisions to appellant's case.

The district court properly declined to apply retrospectively the Redrup and June 12, 1967 decisions of the Supreme Court and the denial of appellant's petition sought on the above ground should be affirmed.

#### CONCLUSION

From the above review of the facts and the law the merit of respondent's position is clear: that the district court did not err by dismissing appellant's petition for a writ, whether considered as coram nobis or habeas corpus, that the court below did not err by refusing to review the habeas corpus proceeding pursuant to appellant's petition for writ of error coram nobis, that the district court did not err by refusing to apply retrospectively the Redrup and June 12, 1967 Supreme Court decisions.

21. Johnson v. New Jersey (1966) 384 U.S. 719 [16 L.Ed.2d 882], Tehan v. Shott (1965) 382 U.S. 406 [15 L.Ed.2d 453], Linkletter v. Walker (1965) 381 U.S. 618 [14 L.Ed.2d 601] and for a general discussion of the principle see Retroactive or Merely Prospective Application, 14 L.Ed.2d 992.

Respondent therefore respectfully submits that the decision of the court below should be approved and its judgment affirmed.

Respectfully submitted,

EDWARD T. BUTLER, City Attorney,

By: /s/ KENNETH H. LOUNSBERRY,  
Deputy

Attorneys for Respondent.

CERTIFICATION

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion the foregoing brief is in full compliance with those Rules.

/s/ KENNETH H. LOUNSBERRY, Deputy.

No. 22,557

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

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AMERICAN CASUALTY COMPANY OF READING,  
PENNSYLVANIA, a corporation,

*Appellant,*

vs.

BERT SIMPSON,

*Appellee.*

---

On Appeal from the United States District Court  
for the Northern District of California

**BRIEF FOR APPELLANT**

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**FILED**

JUN 7 1968

W.M. B. LUCK, CLERK



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No. 22,557

IN THE

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AMERICAN CASUALTY COMPANY OF READING,  
PENNSYLVANIA, a corporation,

vs.

*Appellant,*

BERT SIMPSON,

*Appellee.*

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**On Appeal from the United States District Court  
for the Northern District of California**

**BRIEF FOR APPELLANT**

---

**JURISDICTION**

The amount in controversy exceeding \$10,000.00 and the parties being of diverse citizenship, this action was instituted in the United States District Court for the Northern District of California pursuant to 28 U.S.C.A. § 1332.

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**STATEMENT OF THE CASE**

Appellant, American Casualty Company, issued Group Policy No. VGA 18694 to the City and County of San Francisco which provided accidental death and

dismemberment benefits for all full time employees of the City and County of San Francisco including \$50,000 for the loss of an arm (Ex. B).

Plaintiff and appellee, Bert Simpson, was rehired as a "limited tenure" motorman by the Municipal Railway on May 6, 1963 (Ex. 10; R.T. p. 5). His coverage under appellant's policy was effective as of October 1, 1963 (Ex. 4).

Mr. Simpson last worked for the Municipal Railway on March 16, 1964. Between March 16, 1964, and May 14, 1964, he was on sick leave for a variety of illnesses and bodily injuries. Although medically certified for return to work by May 14, 1964, he testified that he received a telegram on May 12, 1964, notifying him that his mother was seriously ill in Texas and requesting his presence there immediately (R.T. p. 48).

Mr. Simpson immediately went to his supervisor, George Lewis, superintendent of the Potrero Division of the Municipal Railway, and requested a leave of absence to visit his mother in Texas. In accordance with the Civil Service Rules, Mr. Lewis granted Mr. Simpson a ten-day leave to May 22, 1964, which was the maximum leave authorized by the rules for limited tenure appointees (R.T. p. 51, lines 2-23; Ex. 16).

Shortly before the expiration of his leave, Mr. Simpson called from Texas and requested additional leave (R.T. p. 50). Due to his limited tenure capacity, Mr. Lewis was unable to grant Mr. Simpson

any additional leave but suggested that he take his two weeks vacation time which would have extended his authorized absence until June 6, 1964 (R.T. p. 51). Mr. Lewis testified that he at no time stated to Mr. Simpson that he would protect his job for him (R.T. p. 164, lines 15-19).

Mr. Simpson's request for vacation time was subsequently denied by the Personnel Department of the Municipal Railway and he therefore became absent without leave as of May 23, 1964 (R.T. p. 150, lines 17-21). Despite his AWOL status, Mr. Simpson continued to stay in Texas after his leave had expired and was married in Texas on July 7, 1964 (R.T. p. 90).

It was brought to the attention of a Clerk in the Personnel Department of the Municipal Railway on July 9, 1964, that Mr. Simpson had been absent without leave for more than ten days. The Clerk accordingly wrote on the back of Mr. Simpson's original request for leave that Mr. Sandstrom, the acting superintendent of the Potrero Division of the Municipal Railway, had been notified to terminate Mr. Simpson (Ex. A).

On July 21, 1964, while he was still in Texas, Mr. Simpson injured his left hand in a hunting accident; the hand was subsequently amputated (R.T. p. 79).

On July 27, 1964, Mr. Mason (Superintendent of Transportation) notified Mr. Lewis to terminate Mr. Simpson's employment for being absent without leave for ten days. Mr. Lewis carried out this instruction

(R.T. p. 53). A letter confirming the termination was sent to the Civil Service Commission by James K. Carr on August 10, 1964 (Ex. 12). The termination was approved by the Civil Service Commission on October 1, 1964 (R.T. p. 112, lines 5-12; Ex. 13).

Suit was filed by plaintiff and appellee, Bert Simpson, on August 27, 1965, in the United States District Court for the Northern District of California seeking to recover benefits under the Group Policy issued by appellant, American Casualty Company, to the City and County of San Francisco (C.T. p. 1). A Memorandum of Decision finding in favor of plaintiff and appellee Simpson was filed on September 15, 1967 (C.T. p. 56). Judgment was entered accordingly on September 22, 1967 (C.T. p. 58).

This appeal followed.

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#### **QUESTION INVOLVED**

Whether a limited tenure employee of the City and County of San Francisco, who was absent without leave when injured in the State of Texas, and whose discharge was inevitable, is entitled to the benefits of an insurance policy insuring full time employees of the City and County of San Francisco.

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#### **SPECIFICATION OF ERRORS**

1. The District Court erred when it held that appellee was a full time employee of the City and County of San Francisco on July 21, 1964.

2. The District Court erred when it held that appellee was entitled to the benefits of the policy in question.

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### ARGUMENT

**APPELLEE SIMPSON WAS NOT A FULL TIME EMPLOYEE AT THE TIME OF HIS ACCIDENT AND NOT ENTITLED TO THE BENEFITS OF THE POLICY INSURING FULL TIME EMPLOYEES OF THE CITY AND COUNTY OF SAN FRANCISCO**

**Mr. Simpson Was Not Available for Employment.**

One of the tests used by the courts in determining whether an insured was a full time employee is whether the individual was available for work. In *Harlan v. Washington National Insurance Company*, 388 Penn. 88, 130 A. 2d 140 (1957), the insured employee had worked for 40 years for the Consolidated Dressed Beef Company and during the last 25 years of his employment worked as a specialist in the purchase of cattle. In 1952 the insured notified the president of the company that he was not enjoying good health and requested a leave which was granted. During his leave the employee was paid \$100 per month and was consulted frequently by company personnel who respected his judgment and expertise. Four months after the leave was granted the insured died and benefits were refused on the grounds that the insured was not a "full time, permanent employee" at the time of his death.

Affirming judgment for the assured's administratrix the Pennsylvania Supreme Court held that the assured was a full time employee during his approved leave for the following reasons:

"An employee may not actually appear on the premises of his employer for a protracted period of time and still be a full time employee. Such would be true of one who is absent on account of illness, vacation, or for any reason which has the approval of the employer . . . ."

*Harlan v. Washington National Insurance Company, supra, 130 A. 2d 140, 142.*

". . . Full time employment does not mean full time pay. It means being available for full employment; and full employment does not mean a hand at the helm throughout the entire voyage; it means standing by to take over when the exigencies of the passage require the application of one's skill acquired over many journeys of the past. Harlan was standing by when death called."

*Harlan v. Washington National Insurance Company, supra, 130 A. 2d 140, 143.*

The Oregon Supreme Court adopted the above test in *Bakkensen v. The John Hancock Mutual Life Insurance Company*, 222 Ore. 484, 353 P. 2d 558 (1960), and held that a fire watcher who worked irregular hours at the discretion of his employer was nevertheless a full time employee since he was required to be "available" for work during the term of his employment regardless of whether or not he was actually called to work.

The contrast between the above two cases and the situation involving Mr. Simpson is obvious. Mr. Simpson was knowingly and wilfully absent without leave in the State of Texas at the time of his accident on

July 21, 1964, and entirely unavailable for work. His employer, the Municipal Railway of the City and County of San Francisco, had no idea that Mr. Simpson intended to return to the State of California and had no means whatsoever to compel him to work. Mr. Simpson was married on July 7, 1964, almost one and a half months after he became absent without leave and there was no telling when he would return to San Francisco. Clearly Mr. Simpson was not available for work in San Francisco when injured while squirrel hunting in Texas and could not be considered as a full time employee.

#### **Mr. Simpson Did Not Have the Right to Return to Work.**

Another criterion utilized by the courts in determining whether an individual is an employee even though he is not physically performing work for his employer is whether he had a right to return to his position and commence work. *Ballf v. Public Welfare Department*, 151 C.A. 2d 784 (1957), illustrates the point. The Court of Appeal held in *Ballf* that a Civil Service Employee, even though on an approved leave of absence, was still an employee of the City and County of San Francisco and subject to the City's employee residency requirements. In support of their decision the court pointed out that Mr. Ballf held his employment as a matter of right and at any time could return to his position and immediately commence work:

“That petitioner was holding his ‘employment’ is well illustrated by the fact that any time he

desired to terminate his leave he could have returned to his position as a matter of right and the person holding it 'vice Mr. Ballf' would have had to give it up. For all purposes he was an employee of the department except that his leave temporarily excused him from performing his actual duties."

*Ballf v. Public Welfare Department, supra,*  
151 C.A. 2d 784, 788.

The situation confronting Mr. Simpson had he returned to San Francisco and sought reinstatement of his job prior to the accident on July 21, 1964, would have been entirely different than the situation discussed above. Both Mr. Albert (Assistant General Manager of Personnel for the Civil Service Commission) and Mr. Ritchey (Assistant Director of Personnel for the Municipal Railway) testified unequivocally that Mr. Simpson, due to his absence without leave, would not have been entitled to his former job unless he could have produced a doctor's certificate stating that his unauthorized absence was occasioned by illness and medical treatment:

"Q. (Mr. Burdick) Well, the routine procedure was, so we understand each other, your staff would advise the man's nominal head of his department, right?

A. (Mr. Harry Albert) The routine procedure is the correct phrasing of it.

Q. To terminate him?

A. Yes.

Q. And then the administrative procedure would commence, right?

A. That's correct.

Q. Absent this medical certificate, he would be terminated, right?

A. That's correct."

(Page 129, lines 23-25; page 130, lines 1-10.)

"Q. (Mr. Burdick) If came back on, let's say, June 5th and his AWOL status had been achieved by that date—

A. (Mr. Albert) Yes.

Q. —knowing the procedures of both departments, when he came to, let's say, his own operating division, the Municipal Railway, absent a doctor's certificate, such as I have described, they could not put him to work?

A. The Staff of the Commission would not have approved his going back to work absent a sick leave form."

(Page 126, lines 24-25; page 127, lines 1-9.)

. . . . .

"Q. (Mr. Burdick) Now, if Mr. Simpson had presented himself at the Municipal Railway on July 21st, 1964, without a doctor's certificate, which would establish that he himself had been ill or disabled from working, to explain his absence between May 23rd and July 21st, would he have been permitted to go to work?

A. (Mr. Ritchey) He would not have been permitted to go to work until he presented a certificate. We would have asked him to get one."

(Page 151, lines 4-13.)

The reason that Mr. Simpson would have needed a doctor's certificate in order to go back to work after his unapproved absence was explained by Mr. Ritchey in answer to a question propounded by the Court:

"The Court: And why would he have to present the certificate to get back to work?

Mr. Ritchey: Because the rules read that a limited tenure employee is only entitled to ten days personal leave. But he is entitled to sick leave without pay or with pay for the length of time that he is sick."

(Page 151, lines 19 through 25.)

It was stipulated at the time of trial that Mr. Simpson did not stay in Texas because of ill health (page 166, lines 7-8). Mr. Simpson would not have been able to present a doctor's certificate which would have entitled him to return to work and his discharge was therefore a foregone conclusion from the time that he became absent without leave on May 23, 1964. The only remaining question was the date on which his termination papers would be signed.

The evidence disclosed that the bureaucratic machinery needed to effect Mr. Simpson's termination actually began grinding before the accident on July 21st, 1964. Mr. Albert testified that the staff of the Civil Service Commission routinely observed payroll records of Civil Service employees to determine whether or not any of them had become absent without leave. On finding that an individual had fallen into the AWOL status the staff notified the individual's particular administrative head to terminate him (R.T. p. 128).

In Mr. Simpson's case the evidence disclosed that a clerk in Mr. Ritchey's Municipal Railway Personnel Department wrote on the back of Mr. Simpson's

original request for leave dated May 12, 1964 (Ex. A) the following inscription: "7-9-64—Notified Mr. Sandstrom to term.—has not covered sick leave." Although it is not known at whose direction the clerk inscribed the above notation, it is reasonable to suppose that the clerk had been notified by a member of the Civil Service staff that Mr. Simpson was absent without leave and should be terminated. For some unexplained reason, however, Mr. Sandstrom, who was filling in for Mr. George Lewis as the acting superintendent of the Potrero Division of the Municipal Railway failed to terminate Mr. Simpson and instead filled out the discipline report (Ex. 7).

Thereafter the evidence disclosed that the same clerk who had previously spoken to Mr. Sandstrom about Mr. Simpson's termination, requested Mr. Mason, on July 27, 1964, to notify Mr. Lewis to terminate Mr. Simpson for being absent without leave for over ten days (Ex. A). This order was carried out by Mr. Lewis (Ex. 5) and a letter was sent to the Civil Service Commission by Mr. Carr notifying them of the termination. The termination was thereafter approved by the Commission on October 1, 1964.

By his voluntary act in remaining in Texas after his leave had expired, Mr. Simpson effectively terminated his own employment as of May 23, 1964. Mr. Lewis at no time told Mr. Simpson that he would protect his job and Mr. Simpson was fully aware of the consequences of overstaying his leave (R.T. p. 164). The only misapprehension that Mr. Simpson might have been laboring under was that he did not

become absent without leave until June 6, 1964 instead of May 23, 1964, as was actually the case. The confusion over the granting of the two weeks vacation time is of no consequence, however, as Mr. Simpson continued to stay in Texas for approximately six weeks after his alleged vacation time expired.

By voluntarily becoming absent without leave, Mr. Simpson placed himself in the same status as the insured in *Pearson v. Equitable Life Assurance Society of the United States*, 212 N. C. 731, 194 S. E. 661 (1938). The insured in *Pearson* was convicted on July 20, 1936, for a charge of drunken driving and was on that date committed to jail for a term of six months. He died from sunstroke three days later while serving the sentence.

Affirming the denial of the benefits of his group insurance policy the Supreme Court of North Carolina noted that the evidence disclosed that the employer adopted a rule which provided that the employment of any one of its employees would be automatically terminated upon the sentencing of any employee to imprisonment. The decedent was advised of this rule and thus his employment was found to have terminated on the date of sentencing even though he was not advised by his employer of the termination. The employee automatically terminated his status as an employee by his own conduct:

"He knew that he could no longer answer the call of his former employer and that by his own act his status as an employee of the tobacco company had been terminated. Under these circum-

stances no duty rested upon the employer to notify him that the relationship had been discontinued."

*Pearson v. Equitable Life Assurance Society,*  
*supra*, 194 S. E. 661, 663 (1938).

The analogy between *Pearson* and the instant case is obvious. In both instances the employee's conduct terminated his employment and it should not matter when and how the employer stamped the final termination papers for purposes of determining when an insurer's risk had ceased. By providing coverage for only full time employees, the appellant did not intend to cover employees who had left their jobs and were away on unauthorized leaves. If the insurer's coverage is held to be in effect until the employer finally gets around to stamping the last official paper, it is conceivable that a former employee could be covered when shot while attempting to break out of jail for the simple reason that the individual who is responsible for signing the official termination document was home in bed with the flu. Surely the coverage provided by the policy in question should not depend on when an official finally gets around to stamping a piece of paper when it was known to all before the accident that the insured could not return to work and had to be terminated.

**CONCLUSION**

It is respectfully submitted that the judgment of the District Court be reversed and judgment entered in favor of appellant.

Dated, San Francisco, California,

June 4, 1968.

CARROLL, DAVIS, BURDICK & McDONOUGH,

By J. D. BURDICK,

JOHN K. STEWART,

*Attorneys for Appellant.*

---

**CERTIFICATE OF COUNSEL**

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

J. D. BURDICK,

*Attorney for Appellant.*

No. 22,557

FEB 24 1968

IN THE

United States Court of Appeals  
For the Ninth Circuit

---

AMERICAN CASUALTY COMPANY OF READING,  
PENNSYLVANIA, a corporation,  
vs.  
BERT SIMPSON,

*Appellant,*  
*Appellee.*

---

On Appeal from the United States District Court  
for the Northern District of California

BRIEF FOR APPELLEE

---

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OCT 31 1968

WM. B. LUCK, CLERK



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No. 22,557

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

---

AMERICAN CASUALTY COMPANY OF READING,

PENNSYLVANIA, a corporation,

*Appellant,*

vs.

BERT SIMPSON,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California

**BRIEF FOR APPELLEE**

---

Appellee Bert Simpson lost his left arm in a hunting accident on July 21, 1964. He brought suit for accidental dismemberment as an insured under Master Insurance Policy VGA 18694-F issued by Appellant American Casualty Company to the City of San Francisco, his employer. It is undisputed that all premiums were paid, due notice was given and the occurrence was accidental. At the trial Appellant raised as the prime issue the question of whether Appellee was a "full-time Employee" on the date of the injury. The court, sitting without a jury, found that he was and entered judgment on the policy in Appellee's favor in the amount of \$50,000 with interest.

Contrary to required appellate procedure, Appellant's incomplete statement of facts summarizes the evidence favorable to itself, omitting many damaging facts. Hence a more complete statement including evidence favorable to Appellee follows:

#### **STATEMENT OF FACTS**

Appellee, a Civil Service employee, worked as a bus driver for the Municipal Railway (operated by the City and County of San Francisco) from 1946 until he resigned in 1960 (RT 82, 147, 148, Exhibit 10, Exhibit 18). He was rehired in the same position in May, 1963 (RT 44, 82, 108, 115, Exhibits 10, 14). On May 13, 1964, he was granted 10 days personal leave to visit his mother who was "low sick" in Texas (RT 48, 60, 61, 86, Exhibit 7). While there he made at least three telephone calls on different days to George Lewis, his supervisor and superintendent of the Municipal Railway's Potrero Division, requesting extensions of time (RT 50, 51, 61, 63, 74, 87, 91, 93). He believed he was granted additional time by virtue of his two-week vacation leave (RT 50, 88, Exhibit 7). At no time did he intend to quit his job (RT 63-4, 87, 90) and he was reassured he would have a job upon his return (RT 89, 91). His employer's representatives were fully aware of his absence prior to the accident (RT 49, 69-71, 87, 164-165), and continued to carry him on the time rolls as on leave for personal reasons without pay until July 27, 1964, 6 days after his injury (RT 119). There was no rule providing for automatic termination of employment (RT 126). No doctor's certificate for reinstatement of

any sort was required when an employee was absent for personal reasons (RT 73). He was considered a good employee and his supervisor would have been happy to have him back (RT 45, 54). There was no evidence of any request that Appellee present himself for work at any time during his absence.

Appellee lost his arm in a shotgun hunting accident on July 21, 1964 (RT 80-82). On July 27, 1964, some time after being notified of the accident (RT 57), his supervisor, Lewis, took action to end the employment (RT 52, 53) based on Appellee's being on leave for a period in excess of two consecutive working weeks (RT 118, 121, Exhibits 12, 12a, 16). Mr. Carr, the appointing officer, terminated him on the same day (RT 113, 114, 120, Exhibits 12, 12a). The Civil Service Commission approved his termination on October 1, 1964 (RT 112).

Insurance premiums had been paid by payroll deductions and directly by Appellee (RT 41) up to August 15, 1964 (RT 26, 27, 28, 42, 161) to the Edwards Company (RT 41, Exhibit 4), the broker administering the policy for Appellant. The policy was applicable to "all full-time Employees & their spouse (sic)" (Item 5 of Exhibit 9). It provided coverage until "the first premium due date following the date on which the Insured Person ceases to be an employee of the Policyholder" (Part IV of Exhibit 9). It did not define "full-time Employees", nor state whether absence from the job, with or without leave, was a basis for denying coverage (Exhibit 9). Appellant's broker determined if employment existed or if

coverage should be cancelled based upon notification by letter from the Comptroller's office or from the insured himself (RT 34).

Civil Service Commission and Municipal Railway rules provided for termination of a limited tenure employee by the appointing officer upon good cause and subject to approval by the Civil Service Commission (RT 115-117, Exhibit 15). Civil Service Commission Rule 47 stated that

"Appointing officers shall determine whether the absence of a limited tenure appointee is justified or whether the appointment shall be terminated. If the appointment is not terminated, the appointee shall be shown on the time roll as on personal leave without pay." (RT 118).

Miss Loebbing, secretary to the superintendent of the Potrero Division of the Municipal Railway (RT 66, 68), Mr. Harry Albert, Assistant General Manager of Personnel for the Civil Service Commission (RT 123) and Mr. Roger Ritchey, Personnel Officer for the Public Utilities Commission (RT 147) testified the total days absence which would result in termination varied with the particular employee and could depend on the merits of the case. If he returned the day after termination, it might have been put aside and the employee returned to work (RT 66). If he had been away from his job for a period of time, the custom and practice regarding termination was for management to call the division superintendent and have the employee terminated (RT 64-65). This is what was done in the case of Appellee (RT 66).

Every single witness, except Appellant's broker, testified that Appellee was not terminated or fired before July 27, 1964 (RT 45, 52, 53, 66, 111-113, 124, 152). Appellant's broker gave no direct testimony on termination but introduced records showing the insurance effective as of October 1, 1963, and cancelled as of August 1, 1964 (Exhibit 1) with premiums paid to August 15, 1964 (RT 27, Exhibit 4).

The court determined that on the date of loss of the lower portion of his left arm, Appellee "was an employee of the City and County of San Francisco as defined by the terms of the policy; and that plaintiff is entitled to coverage under the terms of the policy." (CT 56).

---

## **ARGUMENT**

### **I**

#### **APPELLANT MUST SHOW THE TRIAL COURT WAS CLEARLY ERRONEOUS.**

The sole task of this court is to determine if there was sufficient evidence supporting the finding and judgment. The burden rests upon the Appellant to convince the court there was not. In *Pacific Queen of Fisheries v. Symes*, 307 Fed. 2d 700 (CA 9th 1962) the court stated at page 706:

"Secondly, it is not incumbent upon *appellees* to persuade this court that the District Court's findings are correct; on the contrary, the *appellants* must persuade this court that the District Court's findings of fact are, as specified by appellants, clearly erroneous. Third, this court must view the

evidence in the light most favorable to the party who prevailed below; such a party must be given the benefit of all inferences that may reasonably be drawn from the evidence. The findings of the Trial Court sitting without a jury must be accepted unless they are clearly erroneous; . . . .”

---

## II

### **EMPLOYMENT WAS NOT TERMINATED UNTIL AFTER THE ACCIDENT.**

The insurance contract contained no provision defining termination of employment, and therefore the issue of employment had to be decided in accordance with the employer's rules.

Premiums were paid, proper notice was given and the loss of Appellee's arm was accidental. There was no contract provision setting forth absence as an exclusion nor any definition of the phrase “full-time Employees”. Accordingly, the court was required to look to the rules of the employer Municipal Railway and Civil Service Commission.

Simpson had been employed as a bus driver for over a year when the July 21, 1964 accident occurred. The first date having any possible effect upon the employee relationship was July 27, 1964. The record is replete with uncontradicted statements by all the representatives of Appellee's employer that he was not terminated before July 27, 1964. This date was arrived at in accordance with the usual custom and practice. Until then, Appellee had been carried on the time

rolls as an employee on leave for personal reasons. Appellee intended to return to work and believed he was eligible. He did not resign, as he did previously, and no evidence was presented indicating any attempt to abandon employment. Medical certificates were not required for an absence for personal reasons, and the employer had no rule of automatic termination. The first action was taken on July 27, 1964, 6 days after the accident, when Appellee's immediate supervisor initiated termination. This termination was not approved until October 1, 1964.

In *McGill v. City and County of San Francisco*, 231 CA 2d 35 (1964), the court held that approval of the Civil Service Commission is required before the services of a limited tenure employee are terminated. The manager of the Municipal Railway had recommended dismissal of a motorman in the Civil Service Commission. The Commission disapproved the termination, but the manager terminated the employment anyway. The employee sought a writ of mandate to compel his reinstatement. In granting the writ and reversing the lower court, the Appellate Court held that the motorman's employment could not be terminated without approval of the Civil Service Commission. They stated on page 38:

“We conclude that the appointing officer may not terminate the employment of a limited tenure employee without the approval of the Civil Service Commission, . . .”

### III

#### APPELLANT'S TESTS FOR EMPLOYMENT STATUS ARE INAPPLICABLE.

##### A. Availability of Employment.

Appellant asserts that availability for work and the right to return to work should be used in deciding if Appellee was an employee at the time of the accident. These tests were urged also to the trial court. The evidence was overwhelming that under the Municipal Railway rules Appellee was an employee at the time of injury, regardless of his availability for work or right to return, and the trial court found accordingly. If it is used as a test, Appellant can still reap no benefit from it. There is no evidentiary support for its argument that Appellee was entirely unavailable for work. The Municipal Railway made no request or hint that he should present himself for work at any time, although they were well aware of his absence. He testified he had no intentions of quitting and believed he was eligible to return to work. This belief was confirmed by the various telephone conversations with his supervisor and his failure to resign as he had done on a prior occasion.

*Harlen v. Washington Nat'l Insurance Co.*, 388 Penn. 1088, 130 Atlantic 2d 140 (1957) now cited by Appellant, but not considered germane by it when cited by Appellee (CT 44), affirmed the determination that employment continued, even though the employee was not engaged at his given job for the full daily and weekly periods which his duties required and the death occurred one month after expiration of his leave. Appellant's cited case of *Bakenson v. The John*

*Hancock Mutual Life Insurance Co.*, 222 Oregon 484, 353 P 2d 558 (1960), also affirmed the judgment for the employee even though he had worked as a fire watcher for only 18 days in the preceding 3 months and the contract required "an employee whose regular working schedule with one employer equals or exceeds 24 hours per week."

#### B. Right to Return to Work.

Appellee's employer carried him on the time rolls until July 27, 1964, did not institute termination until 6 days after the accident, and did not approve termination until over a month after the accident. If he had returned the day following termination it was even possible to have the termination set aside and for him to return to work (RT 66). Appellee's right to return to work is supported by previous court decisions. *Balff v. Public Welfare Department*, 151 CA 2d 784, 312 P 2d 360 (1957), now cited by Appellant but considered as lacking relevance when cited by Appellee (CT 43), also involved a Civil Service Commission employee. At page 788, the court stated:

"The fact that a person is on leave from his 'employment' makes him no less an employee."

While on leave to attend school, Balff continued to be an employee and had to comply with the residency requirements. Balff remained an employee even though he was absent from work.

The previously cited case of *McGill v. City and County of San Francisco*, 231 CA 2d 35 (1964), clearly shows that the services of a limited tenure employee are not terminated until the termination has been approved by the Civil Service Commission.

Appellant has cited the case of *Pearson v. Equitable Life Assurance Society of the United States*, 194 SE 661. There, the employer had a rule that employment automatically terminated upon sentence of an employee to prison. This rule had been specifically brought to the decedent's attention upon a previous arrest. The employer's foreman was notified on the day of sentencing and, as stated at page 662:

“Thereupon the name of the deceased was erased from the roll of employees of the said tobacco company.”

At page 664, the court notes that the deceased employee having, by his own act, terminated his status as an employee and

“. . . the employer having recognized, accepted and acted upon said termination, the defendant is in no way liable to the plaintiff upon this specific suit.” (Emphasis added).

In the case now before the court, there was no rule of automatic termination, the first acts of the employer were on July 27, 1964 and the final acts of termination took place on October 1, 1964. All of this was subsequent to the injury, and accordingly Appellee continued to be an employee at the time of the injury.

Appellant's lack of reference to any specific date or action by the employer ending employment imposes a horrible game of guessing and confusion upon Municipal Railway employees. Appellant would require omniscience in determining when and if employment had been terminated by neglect, design or mistake.

## IV

**BY ITS TERMS, THE POLICY WAS IN EFFECT WHEN  
THE ACCIDENT OCCURRED.**

Regardless of whether Appellee was employed at the time of the accident, he was covered under the terms of the policy. It provided:

- "the individual coverage with respect to any Insured Person shall immediately terminate;
- a. On the date of termination of this Policy by either the Policyholder or the Company as provided in the Termination Part VI (the Company will return the pro-rated portion of any premium contribution unearned as a result of such termination); or,
  - b. On the first premium date *following* the date on which an Insured Person ceases to be an employee of the Policyholder . . . (Part IV of Exhibit 9)" (emphasis added).

All premiums were paid to August 15, 1964 (RT 27, Exhibit 4).

Additionally, the policy required return of any unearned premium as a result of termination. After the accident, premiums were returned and the policy was cancelled as of August 1, 1964 (RT 31, Exhibit 1). By their own acts Appellants thus admit coverage when the July accident occurred. *Quong Tue Sing v. Anglo-Nevada Assurance Company*, 86 C 566, 572.

## V

**CONCLUSION**

The loss of Appellee's arm occurred on July 21, 1964. All representatives of his employer testified that termination did not take place until July 27, 1964, and it was not approved until October 1, 1964. Premiums were paid, notice was given and the injury was accidental. The District Court found Appellee entitled to the promised and paid for benefits. It is respectfully submitted that the judgment in favor of Appellee Simpson and against Appellant American Casualty Company should be affirmed.

Dated, San Francisco, California,  
October 28, 1968.

HOBERT, FINGER, BROWN & ABRAMSON,  
*Attorneys for Appellee.*

No. 22,557

FEB 24 1968

IN THE

United States Court of Appeals  
For the Ninth Circuit

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AMERICAN CASUALTY COMPANY

OF READING, PENNSYLVANIA,  
a corporation,

vs.

*Appellant,*

BERT SIMPSON,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California

REPLY BRIEF FOR APPELLANT

---

CARROLL, DAVIS, BURDICK & McDONOUGH,

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No. 22,557

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

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AMERICAN CASUALTY COMPANY  
OF READING, PENNSYLVANIA,  
a corporation,

vs.

BERT SIMPSON,

*Appellant,*

*Appellee.*

**On Appeal from the United States District Court  
for the Northern District of California**

**REPLY BRIEF FOR APPELLANT**

---

Appellee argues that he continued to be an employee of the San Francisco Municipal Railway at the time of the injury on July 21, 1964 on the grounds that Mr. Mason did not notify Mr. Lewis to terminate him until July 27, 1964. In making this argument, Appellee overlooks the fact that he became absent without leave as of May 23, 1964 (RT 150:17-21) and was not eligible for reinstatement without a medical certificate explaining his absence (RT 126:24-127:9). Inasmuch as Appellee's unapproved absence was not for medical reasons, his discharge was inevitable. All that was uncertain was the timing.

In reply to the foregoing, Appellee argues that the first "acts" of the employer concerning termination took place on July 27, 1964. This argument ignores the testimony of Mr. Albert to the effect that the staff of the Civil Service Commission routinely observed payroll records of Civil Service employees to determine whether or not any of them had become absent without leave. Presumably in response to a call from the Civil Service Commission, a clerk in Mr. Ritchey's personnel department wrote on the back of Mr. Simpson's original request for leave the following inscription:

"7-9-64—Notified Mr. Sandstrom to term.  
—has not covered sick leave." (Exhibit A)

The inscription indicates that Mr. Simpson's employer instituted steps prior to July 21, 1964 concerning his termination, but for some reason Mr. Sandstrom, who was filling in for Mr. Lewis at the time, filled out an additional discipline report instead of terminating Mr. Simpson (Exhibit 7).

In support of his argument that he was a full-time employee of the Municipal Railway and entitled to all the benefits of his employment including his insurance policy during the time that he was absent without leave in the State of Texas, Appellee relies upon the decisions in *Balff v. Public Welfare Department*, 151 C.A.2d 784 (1957) and *McGill v. City and County of San Francisco*, 231 C.A.2d 335 (1964). This reliance is misplaced.

The decision in *Balff v. Public Welfare Department, supra*, is not pertinent as the petitioner in that

case was on an approved leave and still considered to be an employee under the Civil Service requirements as illustrated by his "right" to return to work. By contrast, Mr. Simpson could not return to work as a matter of right and one of his supervisors had been instructed to terminate him two weeks prior to his accident.

The decision in *McGill v. City and County of San Francisco, supra*, does not afford Appellee support in this action as it deals with the question of who has the ultimate authority as between the Civil Service Commission and the appointing officers to terminate Civil Service employees. The special relationship existing between the Civil Service Commission and bodies or agencies subject to its jurisdiction has no bearing on the question of when an insured is entitled to the benefits provided by a private insurance policy.

In a situation such as before this Court where the policy does not specifically enumerate those instances in which an employee will not be considered a "full-time employee", it is only reasonable to adopt certain broad, sensible guidelines as were suggested in Appellant's Opening Brief, namely the availability of employment and the right to return to work. If an individual will be entitled to the benefits of an insurance policy which are predicated upon his status as a full-time employee until such time as the Civil Service Commission approves an order terminating the employee, it places the insuring relationship entirely dependent upon the functioning of the bureaucratic machinery of the Civil Service Commission. Under those

circumstances it would be possible for a former Municipal Railway employee who took a job as a guide in the Swiss Alps to be covered under the terms of the insurance contract simply because the concerned officials never got around to formally entering an order of termination or having it approved. Such a result would be beyond the pale of reason and good sense.

Finally, Appellee argues that he should be entitled to coverage inasmuch as the premiums were paid through August 15, 1964 and the policy provided that individual coverage under the policy terminated "on the first premium date following the date on which an insured person ceased to be an employee of the policy-holder" (Part 4 of Exhibit 9).

This theory is not convincing, however, as the premiums were payable at the rate of \$7.00 per month (Exhibit 4). Since Mr. Simpson became absent without leave on May 23, 1964 and not eligible for reinstatement, his status as an employee for insurance purposes terminated as of that date. The first premium due date following that date was either June 1, 1964 or June 15, 1964, depending on whether Mr. Simpson paid at the first of each month or in the middle of each month.

An employee should not be able to extend his insurance coverage indefinitely without reference to his employment status by the simple expediency of pre-paying his insurance premiums. If that were permissible, a former employee who prepaid his premiums a year in advance would still be covered even though

he had been terminated months before the claim and had moved half way around the world during the interim.

---

### **CONCLUSION**

It is respectfully submitted that the judgment of the District Court be reversed and judgment entered in favor of Appellant.

Dated, San Francisco, California,  
November 25, 1968.

CARROLL, DAVIS, BURDICK & McDONOUGH,  
By J. D. BURDICK,  
JOHN K. STEWART,

*Attorneys for Appellant.*



NO. 22558

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IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

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KENNETH WAYNE CLEAVER,

Appellant,

v.

UNITED STATES OF AMERICA,

Appellee.

---

On appeal from the United States District Court for the  
District of Arizona

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BRIEF FOR APPELLANT

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IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

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NO. 22558

KENNETH WAYNE CLEAVER, APPELLANT

v.

UNITED STATES OF AMERICA, APPELLEE

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On Appeal from the United States District Court  
for the District of Arizona

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BRIEF FOR APPELLANT

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JURISDICTIONAL STATEMENT

Appellant, now released on bond pending appeal, was indicted under 21 U.S.C. 176a and 18 U.S.C. 545 (C.T. 4-5) and, following an unsuccessful motion to suppress, was tried and convicted. The District Court had jurisdiction under 18 U.S.C. 3231. A timely notice of appeal was filed (C.T. 38), giving this Court jurisdiction under 28 U.S.C. 1291.



STATEMENT OF THE CASE

Appellant, who is on release pending appeal, was convicted on a two-count indictment charging, respectively, violations of 21 U.S.C. 176a (receiving, concealing, and facilitating the transportation and concealment of unlawfully imported marijuana) and 18 U.S.C. 545 (unlawfully importing benzedrine tablets), and was sentenced to imprisonment for a period of 5 years on Count I and, concurrently, to a term of two years on Count II. This appeal is based upon the lower court's failure to suppress the marijuana and benzedrine tablets found by Customs officials when, 12 miles north of the Mexican border, the officials stopped the vehicle in which appellant and two other young men, Black and Stewart, were riding.

At the hearing on appellant's pre-trial motion ("M" will be used to refer to the Motion transcript and "T" to refer to the Trial transcript), the Government conceded that, owing to the significant gaps in surveillance, the search in question could not be sustained on border search grounds (M.4); accordingly, the Government undertook the burden of establishing probable cause (M.5). The relevant facts follow:



While at home in Nogales, Arizona at approximately 10 p.m. on the night of July 12, 1967, Turner, a Customs Port Investigator (M.14), received a telephone call from Customs Inspector Larson, who was stationed at the Grand Avenue Port of Entry (M.14). Larson said he had received a call from an informant in Nogales, Sonora, Mexico, who stated that three white American males, two wearing green Army jackets, one wearing a black shirt or sweater, and one or more wearing levis, were in Mexico trying to purchase marijuana (M.7, 18, 27). Nothing was said about the age of the three (M.30-31), about their height and weight (M.18) or about where in the Mexican city they were (M.17), and the informant apparently did not indicate the basis for his conclusion that three Americans were attempting to buy marijuana. Larson told Turner the informer's name (M.7) and Turner recognized the name of the man as one who had provided information some 20-25 times (M.76) over the past 11 or 12 months (M.14-15), the information proving to be reliable in approximately 60% of the cases (M.72, 76).

Turner went immediately to the Port of Entry, called Agent Washington, and asked Washington to meet him at the Port. (M.16, 46). When Washington arrived, Turner told him



of the call Larson had received (M.46); Washington remained at the Gate while Turner went into Mexico to investigate (M.46). When Turner had been in Mexico for about 15 minutes (at about 10:30 p.m.) (M.18-19), the informant again called the Port. Speaking to Washington, the informant said, "They have jumped the fence up by the cemetery, by the Mexican cemetery with a bag of marijuana" (M.47). Washington recognized the voice of the informant as the same person that had called Larson (M.47) and Washington immediately established radio contact with Turner and told him of the message (M.48,8). Neither Washington nor Turner personally saw anyone jump the fence (M.20, 31), and the informant did not say that he saw the young men cross the border, nor did he disclose any underlying facts or circumstances that led him to conclude that they had done so (M.47; see also M.76-77).

As a result of the radio message from Agent Washington, Turner returned to the United States (M.8) and proceeded to the end of the chain link fence, which is three miles west of town, in pursuit of the men (M.66). Finding no sign of them, Turner returned to Mexico in an attempt to locate the informer; he did so, and the informer told him the men had been dealing with a certain individual, that they had a bag, and that they



had crossed the fence (M.66).

The informer did not tell Turner there had been a buy from the individual--only that the men had contacted him (M.68-69). He did not say that he personally observed a sale or even a suspected transaction between the individual and the Americans, or that he had spoken with that man (M.69-70)<sup>1</sup>--and Turner did not seek to discover the facts upon which the informant based his conclusion that the three men had been in contact with the individual (M.76-77). The informant did not say that he personally saw the men go over the fence, and again Turner did not ask about the basis for the informant's conclusion (M.76-77). Nor did the informant indicate whether he himself had a different source of information regarding the supposed sale and regarding the fence crossing, and Turner did not go into that with him (M.76-77).

After speaking with the informer, Turner returned to the United States, and this time drove west on International Street, which parallels the international fence for approximately one mile (M.66-67; M-9; T-23), and which then leads

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<sup>1</sup> Although Turner suspected that individual to be a seller of narcotics, Turner never had any personal contact with him, and he was not an informer for the Customs Office (M.69).



to a path passable by pedestrians (M.21). As he drove into the area, Turner noticed two young men near the end of the road walking east towards town (M.66-67; M.9).

One of the young men was wearing an olive Army jacket, the other a black sweater (M.9). Turner came within three feet of the two and could see them rather clearly (M.23-24); although it had rained earlier in the evening, he did not notice any dirt or moisture on their clothing (M.25), and did not think they were walking in a suspicious manner (M.25, 39). The area along International Street is residential, with houses extending all the way to the west end of the street (M.38; T.39). There are six houses in the immediate vicinity (T.53, 54, 68).<sup>2</sup>

Turner, in his unmarked car with a 5-foot police radio aerial (M.23-24), drove right past the two men, proceeded to the west end of International Street, turned around, drove past the men again, parked his car somewhat further east, and got out of his car in order to follow the men on foot. (M.23, M.9; T.24). He followed them for about five blocks (M.9)

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<sup>2</sup>On the Mexican side of the fence is a street with houses and quite a bit of light (T.68-69).



through a very well lighted and heavily populated area (T.73-76); they were walking on the sidewalks in an average manner and were not carrying anything (T.73-76).

Next, the two men entered a red Falcon Ranchero bearing California plates, and drove off (M.10). Turner lost surveillance for approximately a minute (M.40-41) while he ran back to his own car, but then followed the Ranchero, which returned to the area near the fence (M.10). For a period of about four minutes, during which time the Ranchero was stopped in a residential area (M.43) near the fence, Turner, who was 1/2 mile away from the Ranchero (M.43), lost sight of it and could see only reflections of light (M.42; T.26). Then, the Ranchero drove back past Turner (M.10), and he noticed that there were then three persons in it--but he saw merely three heads and could not recognize any of the three persons (M.34; T.26, 57-58). Turner followed the Ranchero for a few blocks, but when it turned south, Turner proceeded north on Grand Avenue to a spot where Agent Washington and Agent-in-Charge Cameron were waiting (M.48, 50; T.27).

No agent took up surveillance of the Ranchero when Turner left it (M.11, 36-37; T.27), and it was not again seen until some 10-15 minutes later when Agent Swindler--a Customs Agent



stationed slightly south of the spot where Washington, Turner and Cameron were waiting (M.85)--noticed the Ranchero pass him going north (M.49). Swindler alerted Washington (M.49), and Washington and Cameron followed the vehicle in Washington's car (M.50). Turner apparently followed the Ranchero in his own car (M.11, 37), as did Swindler (M.85-86).

After driving for approximately one mile, the Ranchero made a U-turn and parked in front of a closed Richfield Station at the curb of a main street which had traffic even at that time of night (M.11; T.96-98). The agents all continued north for a short while and then pulled off the highway to wait (M.11, 50, 85-86). After a while, Swindler returned south to investigate and drove past the service station where he noticed the three men standing near the soda machine. In a few minutes, Swindler was contacted by the other agents and was told that the Ranchero was again proceeding north (M.86). The Ranchero had been free from surveillance for 15-20 minutes while parked at the Richfield Station (M.37). Swindler, upon request of the agents (M.86), went to the service station to see if anything had been left there; he discovered nothing, reported that to Washington and Cameron, and then drove north and caught up with the vehicles driven by his colleagues (M.86).



The Ranchero was stopped by Agents Washington and Cameron 12 miles north of Nogales, Arizona (M.12). When he stopped the vehicle, Washington knew only that there were three persons in it--he could not see or identify the occupants or their clothing (M.59-60). All three men were in shirtsleeves when stopped (M.39;T.34). Stewart was driving (M.13). A search that followed the stopping of the vehicle revealed the marijuana and the benzedrine tablets (T.30) that were the subject of the motion to suppress.



SPECIFICATION OF ERRORS RELIED ON

1. The District Court erred in failing to suppress evidence obtained from appellant pursuant to a search which was not a border search and which was not based on probable cause.



QUESTIONS PRESENTED

1. Whether a search 12 miles from the Mexican border can be sustained as a border search where surveillance was not continuous and where the Customs officials had neither actual knowledge nor probable cause to believe that appellant had crossed the international border.
2. Whether there was probable cause for a search where Customs officials acted upon an informant's communication but were not informed of the facts and circumstances which led the informant to conclude that three men had crossed the border carrying marijuana.



### SUMMARY OF ARGUMENT

Appellant's conviction must be reversed because of the lower court's failure to suppress evidence obtained from appellant in a search conducted several miles from the international border which cannot be sustained as a border search and which was not based on probable cause.

As the Government correctly conceded below, the search in question was not a border search. A border search will not be found unless there is virtually continuous surveillance from the time of border crossing until the time of search. Leeks v. United States, 356 F.2d 470, 471 (9th Cir. 1966); King v. United States, 348 F.2d 814, 816 (9th Cir. 1965). But in the present case, the officers who stopped appellant were not certain that he was the same person who they suspected had crossed the border, and, in addition, appellant was not under surveillance for some forty minutes during the two-hour period from when he was first seen until he was stopped. Moreover, no Customs official or informant saw appellant cross the international border, and the officials, who relied on the bare conclusory statement of an informant, did not even have probable cause to believe that such a crossing took place. Aguilar v. Texas, 378 U.S. 108, 84 S.Ct.



1509 (1964). Thus the search cannot be classified as a border search.

Nor was the search based on probable cause. A 60% reliable informant told the Customs officials that three men had crossed the fence carrying marijuana. But since the informant did not disclose the facts and circumstances underlying his conclusion, the officials clearly could not have obtained a warrant in this case. Aguilar v. Texas, supra. And since the requirements for proceeding without a warrant are at least as high--and probably higher--than the requirements for proceeding with a warrant, the warrantless action of the Customs officials was in plain violation of the Fourth Amendment, and the resulting evidence should have been suppressed. Wong Sun v. United States, 371 U.S. 471, 479-80 (1963); Beck v. Ohio, 379 U.S. 89, 96 (1964); United States v. Soyka, No. 31583 (2d Cir., decided June 18, 1968).



## ARGUMENT

I. The search 12 miles from the Mexican border cannot be sustained as a border search where there were significant gaps in surveillance and where the Customs officials had neither actual knowledge nor probable cause to believe that appellant had crossed the international border.

At the hearing on the motion to suppress, the Government properly conceded that the gaps in surveillance preceding the search at issue foreclosed the possibility of classifying the search as a "border search" (M.4). That concession was clearly called for: Before invoking the label "border search" to condone a search based on mere suspicion, this Court has rightly and repeatedly required a showing of virtually continuous surveillance from the time of border crossing until the time of search. Leeks v. United States, 356 F.2d 470, 471 (9th Cir. 1966);<sup>3</sup> King v. United States, 348 F.2d 814, 816

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<sup>3</sup>"The enterprise of officers 'tailing' Leeks was continuous from the time Leeks crossed the border until he was stopped by the command of Customs officers. (There was a shift in who pursued Leeks, brought about by intercommunication of officers over their radios). Although there was a period when Leeks, as he drove, may have been momentarily out of the sight of all of the officers, there was no breach in the continuity of the project of the officers following him." (Emphasis supplied).



<sup>4</sup>  
(9th Cir. 1965). See also Rodriguez-Gonzalez v. United States,  
378 F.2d 256 (9th Cir. 1967); Alexander v. United States, 362  
F.2d 379 (9th Cir. 1966); Contreras v. United States, 291 F.2d  
63 (9th Cir. 1961). The undisputed facts of the instant case  
plainly establish the absence of the requisite surveillance.

It will be recalled that when Agent Turner followed  
the two young men, they entered a Ranchero, drove west on  
International Street, and stopped for a period of approximately  
four minutes. During that four-minute period, Turner was  
1/2 mile away from the Ranchero and lost sight of it (M.42-43).  
While that time period is admittedly short, it is nevertheless  
significant, for when the Ranchero returned from that spot, it  
had three occupants--none of whom was ever again recognized  
by Turner or any other official until the vehicle was  
eventually stopped (M.34, 59-60; T.26, 57-58)! That gap in  
surveillance should itself defeat a border search, for the

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<sup>4</sup> "We hold that where, as here, duly authorized officers receive information that a person or vehicle is about to cross the border with contraband in violation of the laws of the United States, and where shortly thereafter a person or vehicle conforming substantially to the description thereof given to such officers is seen to cross the border, and where such person or vehicle is followed therefrom by said officers and kept under surveillance until stopped and searched, ... such search may be held to be a border search." (Emphasis supplied).



agents knew the Ranchero had not been in Mexico and, because of the inadequate surveillance, the agents had no way of knowing whether the persons they stopped were the same persons who had allegedly been in Mexico.

Furthermore, the above gap in surveillance does not stand alone. Equally significant is the fact that after the Ranchero left International Street with three occupants, no one kept the vehicle under surveillance, and it was out of sight for perhaps 15 minutes (M.11, 36-37, 49; T.27). And, just a short time later, when the vehicle made a U-turn and parked at the Richfield Station, surveillance stopped for about 20 minutes (M.37). In other words, during the two-hour period from when the men were first seen until they were stopped, they were out of sight for about forty minutes.<sup>5</sup>

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<sup>5</sup>The two-hour time period--from 10:45 p.m. to 12:45 a.m.--is an approximate calculation. At 10:30 p.m., Turner was in Mexico and received a call from Agent Washington that three men had jumped the fence. He went into the United States, found nothing, returned to Mexico to find the informer, again returned to the United States, and then first spotted the two men walking. It can be safely assumed that at least 15 minutes elapsed in the interim. At 12:15 a.m., the Ranchero was seen leaving the city (M.85). It parked for approximately 20 minutes at the Richfield Station, and was then stopped on a highway 11 miles from town. That time would be approximately 12:45 a.m.



Under such circumstances, a border search cannot be sustained.

There exists still another surveillance gap which, independent of the others, is fatal to any border search contention: No Customs official observed appellant and the other men cross the border--the period most crucial for border search purposes (M.20,31). That factor alone renders vulnerable a search based on less than probable cause, for it is clear that surveillance at the time of entry into the United States is necessary in order for a valid border search to be found. See, e.g., Leeks v. United States, supra at 471 and King v. United States, supra at 816, quoted, respectively, in footnotes 3 and 4 of this brief.

Moreover, it is clear that in the present case the Customs officials not only lacked the required actual knowledge of a border crossing, but did not even possess probable cause to believe that such a crossing occurred: the informant did not disclose to the officials any underlying facts or circumstances that led him to conclude that the men had crossed the border, and the indications are that he himself relied on hearsay in so concluding (M.47, 76-77). On those facts, a finding of probable cause of border crossing is plainly precluded. Aguilar v. Texas, 378 U.S. 108, 84 S.Ct.



1509 (1964). (The use of an informer's communications to establish probable cause is discussed in detail in the next section of this brief). And it would, of course, be constitutionally impermissible to sustain on border search grounds a search conducted on "mere suspicion" that a person has crossed the international boundary: condonation of such a practice would drastically dilute the Fourth Amendment rights of American border community residents and visitors, for it would continually subject them to the possibility of detentions and searches at the mere whim of Customs officials. Cf.

Carroll v. United States, 267 U.S. 132, 154 (1925); <sup>6</sup> Marsh v.

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"Travelers may be...stopped in crossing an international boundary because of national self-protection reasonably requiring one entering the country to identify himself as entitled to come in, and his belongings as effects which may be lawfully brought in. But those lawfully within the country, entitled to use the public highways, have a right to free passage without interruption or search unless there is known to a competent official authorized to search, probable cause for believing that their vehicles are carrying contraband or illegal merchandise."

In addition, a strong showing that a person or his belongings crossed the border should be required because, as this Court has recognized, "the primordial purpose of a search by Customs officers is not to apprehend persons, but to seize contraband property unlawfully imported or brought into the United States." Alexander v. United States, supra, at 382.



United States, 344 F.2d 317, 325 (5th Cir. 1965). Appellant is, of course, assuredly not suggesting that the Customs official would so act; it is suggested only that such a decision would unjustifiably leave open the possibility for such an arbitrary and unchecked exertion of power.

II. Since the Customs officials were not informed of the underlying facts and circumstances which led the informant to conclude that three men had crossed the border carrying marijuana, the subsequent search was not based on probable cause.

Since the Government, at the motion to suppress, recognized that its actions in stopping and searching the vehicle could not be sustained on a border search theory, it attempted to justify its behavior by proving probable cause (M.5). The burden of proving probable cause rests, of course, with the Government, Cervantes v. United States, 278 F.2d 350 (9th Cir. 1960), and it is evident from the record that the burden was not adequately discharged.

In stopping and searching the vehicle in which appellant was riding, the Customs officials relied heavily upon



an informant's conclusion that three persons had contacted a certain individual and had crossed the fence with a bag of marijuana (M.7, 18, 27, 47, 66). And the officials acted on those bare conclusory statements, without inquiring about the basis for the informant's belief. The informant, for instance, never indicated that he even saw the three men at all, let alone that he saw them purchasing marijuana or crossing the fence with it (M.47, 66, 68-70, 76-77). It seems, in fact, that the agents did not think the informant possessed first-hand knowledge of any of those events; the informant seemingly had his own source or sources of information concerning the transaction and the border crossing (M.76-77), and the identity and reliability of those sources--and the means by which they learned of the events--were not disclosed to the officials. As will be demonstrated below, probable cause could not have existed for the search, for an officer is not permitted to use the communication of an informant as an element of probable cause unless he has been informed of--and has evaluated--some of the circumstances underlying the informant's conclusion.

Aguilar v. Texas, supra.

Aguilar dealt, of course, with the use of an informant's communication in obtaining a warrant. To insure that magistrates, in determining probable cause, perform their required



neutral and detached fact-finding function instead of in effect delegating that decision to law enforcement officers, the Supreme Court in Aguilar enunciated the following constitutional test:

"Although an affidavit may be based on hearsay information and need not reflect the direct personal observations of the affiant, the magistrate must be informed of some of the underlying circumstances from which the informant concluded that the narcotics were where he claimed they were, and some of the underlying circumstances from which the officer concluded that the informant...was 'credible' or his information 'reliable'. Otherwise, 'the inference from the facts which lead to the complaint' will be drawn not 'by a neutral and detached magistrate,' as the Constitution requires, but instead, by a police officer 'engaged in the often competitive enterprise of ferreting out crime, or as in this case, by an unidentified informant."

378 U.S. at 114-15 (citations omitted).

When a warrant is sought, therefore, "the Commissioner must judge for himself the persuasiveness of the facts relied on by a complaining officer to show probable cause. He should



not accept without question the complainant's mere conclusion that the person whose arrest is sought has committed a crime." Giordenello v. United States, 357 U.S. 480, 486, 78 S.Ct. 1245 (1958). And although an affiant seeking a warrant may rely on an informant's hearsay remarks rather than on personal knowledge, the Commissioner's function of evaluating probable cause remains the same, and therefore the affiant must present the Commissioner with sufficient facts to enable the latter to conclude that the informant is a reliable person who has a basis for his conclusion. Aguilar v. Texas, supra; Jones v. United States, 362 U.S. 257, 269, 80 S.Ct. 725 (1960).

Had the Customs officials in the present case sought a warrant to search the Ranchero and its occupants, they undoubtedly would have been turned away for failing to meet the constitutional standards set by Aguilar: their hearsay source was hardly reliable--having given inaccurate and unreliable information 40% of the time in the past (M.72, 76)--and, in any event, they did not know of any underlying facts and circumstances upon which the source based his conclusion.<sup>7</sup>

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<sup>7</sup> And the officers clearly could not have obtained a warrant on the basis of the facts within their personal knowledge--facts apart from the informant's communication. (continued next page)



Had a Commissioner erroneously issued a warrant to the officials, an appellate court, in reversing, might correctly employ language at least as strong as the following statement in Aguilar:

"Here the 'mere conclusion' that petitioner possessed narcotics was not even that of the affiant himself; it was that of an unidentified informant. The affidavit here not only 'contains no affirmative allegation that the affiant spoke with personal knowledge of the matters contained therein,' it does not even contain an 'affirmative allegation' that the affiant's unidentified source 'spoke with personal knowledge.' For all that appears, the source here merely suspected, believed or concluded that there were narcotics in petitioner's possession. The magistrate here certainly could not 'judge for himself the persuasiveness of the facts relied on...to show probable cause.' He necessarily accepted 'without

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Although some of those circumstances are conceded slightly suspicious, they are wholly insufficient to meet the high probable cause standard, and, moreover, as the Statement of the Case indicates, the facts and circumstances were generally innocuous and consistent with innocence (e.g., the young men walked in a non-suspicious normal manner through a residential section, etc.).



question' the informant's 'suspicion,' 'belief' or 'mere conclusion.'"

378 U.S. at 113-14.<sup>8</sup> Put another way, since a warrant assuredly would not be forthcoming if an officer-affiant merely said, "I have been incorrect 40% of the time, but I honestly believe X has unlawfully imported marijuana," a fortiori the warrant would not issue if the affiant's belief was derived from a conclusory remark of an anonymous informer of equal unreliability. Jones v. United States, supra, at 269.

The present case differs from Aguilar because the search in question was conducted without a warrant. But certainly the difference is meaningless in terms of legal consequence, because it is established beyond any doubt that the requirements for arresting or searching without a warrant are at least as stringent as the requirements for procuring a warrant, Wong Sun v. United States, 371 U.S. 471, 479-80

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<sup>8</sup> Since in the present case, unlike Aguilar, there is an affirmative indication that the informant did not himself speak with personal knowledge, even stronger reversing language might appropriately be employed.



(1963)<sup>9</sup>, Beck v. Ohio, 379 U.S. 89, 96, 85 S.Ct. 223 (1964),

and are in fact probably even more stringent. United States v. Ventresca, 380 U.S. 102, 85 S.Ct. 741 (1965).

Although, surprisingly, the majority of one panel disagreed, Smith v. United States, 358 F.2d 833 (D.C.Cir. 1966) (divided court)<sup>10</sup>, all other cases considering the issue that have come to counsel's attention have correctly followed

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<sup>9</sup>"Whether or not the requirements of reliability and particularity of the information on which an officer may act are more stringent where an arrest warrant is absent, they surely cannot be less stringent than where an arrest warrant is obtained. Otherwise, a principal incentive now existing for the procurement of arrest warrants would be destroyed."

<sup>10</sup>The majority in Smith felt that Aguilar did not modify Draper v. United States, 358 U.S. 307, 79 S.Ct. 329 (1959), and found sufficient facts present to sustain a finding of probable cause under Draper. But Smith is incorrect in finding Draper unaltered by Aguilar: Draper is modified to the extent that it would permit probable cause to be shown solely by the probable reliability of the informant. Aguilar, in other words, represents a synthesis of Draper (re the reliability of the informer) and Jones v. United States, supra (re the basis for the informer's belief), and both prongs of the test must now be satisfied if an informer's hearsay communication is to be considered as a proper ingredient of probable cause.

But even if Draper remains entirely intact, its high standard was certainly not nearly met in the present case: Draper involved a highly reliable (100%) informant, who provided a wealth of detail in his communications, accurately predicting the suspect's subsequent course of activities, and who, inferably, had personally followed the course of the suspect's activities over a period of time. None of those significant factors are found in the current case.



the guidance of Wong Sun and Beck and have found the Aguilar probable cause standards applicable to non-warrant situations.

See United States v. Soyka, No. 31583 (2d Cir., decided Jan. 18, 1968); McCray v. Illinois, 386 U.S. 300, 87 S.Ct. 1056 (1967); Townsley v. United States, 215 A.2d 482 (D.C.Ct.App.1965); Perry v. United States, 336 F.2d 748 (D.C.Cir.1964); Jackson v. United States, 336 F.2d 579, 580 (D.C.Cir.1964): "Thus the court, in determining probable cause, like the magistrate issuing a warrant, must be informed of the underlying circumstances from which the officers concluded that the informant was credible or his information reliable. And the evidentiary requirements are greater when, as here, a warrant is absent."<sup>11</sup> The Supreme Court recently removed any doubt that might have existed in this area when it applied the Aguilar test to a non-warrant situation. McCray v. Illinois, supra, at 304.

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<sup>11</sup> Giordenello, supra, at 486, warned that a U.S. Commissioner "should not accept without question the complainant's mere conclusion that the person whose arrest is sought has committed a crime." In non-warrant cases growing out of informants' communications, the situation is even more severe: Instead of a magistrate accepting the conclusion of an officer, the situation develops into one where both the officer and the district court accept, in effect, the blanket conclusion of an informant.



"The threshold question in this case, therefore," as in Wong Sun, "is whether the officers could, on the information which impelled them to act, have procured a warrant..."

Wong Sun v. United States, supra, at 480. We have seen that they unquestionably could not have. The most recent ruling in this area of the law--the Second Circuit case of United States v. Soyka, supra--is also the decision most directly relevant to the case at hand. In Soyka, an informant whose past information had on several occasions proven accurate, telephoned agents of the Federal Bureau of Narcotics and told them that Frank Soyka, whom he described in great detail, lived in Apartment 54 of a certain dwelling and was selling heroin from his apartment. The caller also said Soyka had in the past been arrested on three specified charges and had recently disconnected his phone; after the call, the agents verified that information. The next day, the informant again called and said Soyka at that time had heroin in his kitchen cabinet. The agents then went to Soyka's apartment building for the purpose of verifying the location preparatory to seeking a search warrant. When they approached the floor on which Apartment 54 was located, the door to the apartment opened and Soyka--who matched the informant's description--walked out but then noticed one of the agents and, looking



startled, jumped back to the apartment. Soyka was immediately arrested, and the ensuing search disclosed heroin in his kitchen cabinet.

Reversing Soyka's narcotics conviction, Judge Smith, speaking for himself, for Judge Waterman, and, presumably, for Judge Friendly,<sup>12</sup> recognized that a warrantless arrest must minimally meet the standards for obtaining a warrant, and that "on this record, the agents...could not have constitutionally obtained a warrant for the search of Soyka's apartment, because they were not aware of the underlying circumstances from which their anonymous informant concluded that the narcotics were in Soyka's kitchen cabinet." Slip op. at 1094. And "although probable cause may be based on hearsay testimony, that testimony must be based on the personal observation of the absent witness" or, at least, upon the personal observation of the first link in a chain of reliable informants. Id. at 1096. Soyka's reasoning would clearly call for a reversal in the instant case. Moreover, the case at hand presents in at least two respects a substantially stronger case for

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<sup>12</sup>Judge Friendly dissented, but seemingly concurred on the point in question. Slip op. at 1103.



reversal than did Soyka: (1) the severely suspicious conduct of Soyka was hardly matched by appellant and his companions; (2) the agents in Soyka could almost have inferred that their informant spoke with personal knowledge gained from observation of the premises, see slip op. at 1103-04 (opinion of Judge Friendly), while the agents in the present case assumedly thought their informant derived his information from some other unidentified source.

That a reversal is called for in this case is, no doubt, attributable not to any overstepping on the part of the Customs officials, but rather to the fact that the present structure of the law enforcement system in the area involved is probably geared almost exclusively to border searches, posing problems in those occasional cases where, as here, an arrest or search must fall unless supported by probable cause. When the concept of a border search forms the underpinning of a law enforcement system, there is indeed little reason, in the absence of specific guidance, for any part of that system--officer or informant--to be overly concerned about some of the more technical aspects of the probable cause concept.

Since Customs officials assumedly know, for example,



that a border search will be sustained even if based on a vague or stale communication, Cervantes v. United States, supra, at 353 (dictum), or on a tip from an unreliable informant, Hammond v. United States, 356 F.2d 931 (9th Cir. 1966), they will not ordinarily be concerned with the circumstances underlying an informer's conclusion or with the informer's reliability. Similarly, when a legitimate border search will usually follow his communication, an informant--particularly if his compensation is determined by the number of contraband seizures resulting from his tips<sup>13</sup>--has little to lose and everything to gain by giving voice to rumors and by alerting officials whenever he merely suspects or believes someone to possess contraband--even if his conclusion is based on the fact that "he heard it from someone who knew somebody whose brother had bought heroin..." United States v. Soyka, supra, slip op. at 1096.

The apparent willingness of Customs officials to accept

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<sup>13</sup> See, e.g., the payment provision of 21 U.S.C. §199:  
The Commissioner of Narcotics is authorized and empowered to pay any person, from funds now or hereafter appropriated for the enforcement of the narcotic laws of the United States, for information concerning a violation of any narcotic law of the United States, resulting in a seizure of contraband narcotics, such sum or sums of money as he may deem appropriate... (Emphasis supplied).



the conclusions of their informants without probing into the facts and circumstances underlying those conclusions, is, as we have seen, understandably triggered by the great prevalence of border searches, and is of little consequence when border searches result. But since that same lack of inquiry will lead to reversal in those instances where the resulting search cannot be categorized as a "border search", it would seem that the arrests and searches requiring probable cause could often be upheld if the Customs officials were advised, as a precautionary measure, to ask one simple question of informants who state mere conclusions: "How do you know?" If the response is anything similar to "I have seen," United States v. Soyka, supra, slip op. at 1104 (opinion of Judge Friendly), a later search may well be sustained even if it fails to qualify as a border search. Perhaps the present case is a proper vehicle for providing the necessary guidance.

#### CONCLUSION

For the reasons stated, it is respectfully submitted  
that the judgment of conviction be reversed.<sup>14</sup>

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<sup>14</sup> Reversal is clearly the remedy called for. Since a remand



CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

  
\_\_\_\_\_  
David B. Wexler  
Attorney for Appellant

---

would be inappropriate even in a case where the record is unclear concerning what facts the informant communicated, Beck v. Ohio, supra, at 97, the remand technique would be clearly uncalled for where the record shows specifically the absence of a crucial communication.



CERTIFICATE OF SERVICE BY MAIL

I, DAVID B. WEXLER, declare that I served three copies of the attached Brief for Appellant by mail on April 3, 1968, on Jo Ann D. Diamos, Office of the United States Attorney, P. O. Box 1951, Tucson, Arizona 85702.

David B. Wexler

David B. Wexler  
Attorney for Appellant



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IN THE  
United States Court of Appeals  
FOR THE NINTH CIRCUIT

KENNETH WAYNE CLEAVER,  
*Appellant,*

vs.

UNITED STATES OF AMERICA,  
*Appellee.*

} No. 22,558

On Appeal from the Judgment of  
The United States District Court  
For the District of Arizona

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BRIEF FOR APPELLEE

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EDWARD E. DAVIS  
United States Attorney  
For the District of Arizona

FILED

JO ANN D. DIAMOS  
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Attorneys for Appellee

MAY 2 1968

WM. B. LUCK, CLERK





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IN THE

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**BRIEF FOR APPELLEE**

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**I.**

**JURISDICTIONAL STATEMENT OF FACTS**

The Government accepts and adopts the Jurisdictional Statement of Facts of Appellant with the following additions:

Count I of the Indictment charged Appellant Kenneth Wayne Cleaver, David Luke Stewart, with receiving, concealing and facilitating the transportation and concealment of approximately ten and one-half pounds of bulk marijuana contrary to law, and which they knew had been imported contrary to law, all in violation of 21 U.S.C.A. §176a.

At trial, Appellant had retained counsel; on Appeal different counsel was appointed under 18 U.S.C.A. §3006A; on the day of trial, defendant Black was granted severance for trial from Appellant Kenneth Wayne Cleaver (Reporter's transcript of trial, page 6. Hereinafter the Clerk's Record will be referred to as "RC"; the reporter's transcript of testimony at the hearing of the Motion to Suppress will be referred to as "M RT" and the reporter's transcript of the testimony at trial will be referred to as "RT"; the number following will refer to the page, and the number following "L" will refer to the line. Appellant Kenneth Wayne Cleaver will be referred to as Cleaver or Appellant.)

## II.

### STATEMENT OF FACTS

While at home in Nogales, Arizona, at approximately 10 p.m. on the night of July 12, 1967, Turner, a Customs Port Investigator (M RT 14), received a telephone call from Customs Inspector Larson, who was stationed at the Grand Avenue Port of Entry (M RT 14). Larson said he had received a call from an informant in Nogales, Sonora, Mexico, who stated that three white American males, two wearing olive drab or green Army jackets, one wearing a black shirt or sweater, were in Mexico trying to purchase marijuana. (M RT

7) Nothing was said about the age of the three (M RT 30-31), about their height and weight (M RT 18) or about where in the Mexican city they were (M RT 17), and the informant apparently did not indicate the basis for his conclusion that three Americans were attempting to buy marijuana. Larson told Turner the informer's name (M RT 7) and Turner recognized the name of the man as one who had provided information some 20-25 times over the past 11 or 12 months (M RT 14-15), the information proving to be reliable in approximately 60% of the cases (M RT 72).

Turner went immediately to the Port of Entry, called Agent Washington, and asked Washington to meet him at the Port (M RT 16, 14). When Washington arrived, Turner told him of the call Larson had received (M RT 46); Washington remained at the Gate while Turner went into Mexico to investigate (M RT 46). When Turner had been in Mexico for about 15 minutes (at about 10:30 p.m.) (M RT 18-19), the informant again called the port. Speaking to Washington, the informant said, "They have jumped the fence up by the cemetery, by the Mexican cemetery with a bag of marijuana" (M RT 47). Washington recognized the voice of the informant as the same person that had called Larson (M RT 47) and Washington immediately established radio contact with Turner and told him of the message (M RT 8, 48). Neither Washington nor Turner personally saw anyone jump the fence (M RT 20, 31), and the informant did not say that he saw the young men cross the border, nor did he disclose any underlying facts or circumstances that led him to conclude that they had done so ( M RT 47; 76-77).

As a result of the radio message from Agent Washington, Turner returned to the United States (M RT 8) and proceeded to the end of the chain link fence, which is three miles

west of town, in pursuit of the men (M RT 66). Finding no sign of them, Turner returned to Mexico in an attempt to locate the informer; he did so, and asked the informer if he was sure they had crossed the fence and the informer replied he was sure (RT 66) and told him the men had been dealing with a certain individual, Gradillas, that they had a bag, and that they had crossed the fence (M RT 66). Gradillas was known to the agent as a dealer in narcotics and marijuana (M RT 69, L 13-14 and 18).

The informer did not tell Turner there had been a buy from Gradillas—only that the men had contacted Gradillas (M RT 69). The informer did not say that he personally observed a sale (M RT 69-70), nor did the informer tell the Agent how he had occasion to know Gradillas (M RT 69-70). Turner did not go into the basis of the informer's knowledge since he left immediately to get back across the Line (M RT 76-77).

After speaking with the informer, Turner returned to the United States, and this time drove west on International Street, which parallels the international fence for approximately one mile (M RT 66-67; RT 23), and which then leads to a path in the brush passable by pedestrians (M RT 21). As he drove into the area, Turner saw, at a point one-half mile west of the port, two young men walking from the brush at the end of the road walking east towards town (M RT 8-9).

One of the young men was wearing an olive drab Army jacket, the other a black sweater (M RT 9). Turner came within three feet of the two and could see them rather clearly (M RT 23-24); the area they were walking in would make Turner suspicious (M RT 24). The area along International Street is residential, with houses extending all the way to the west end of the street (M RT 37; RT 39). There are six

houses in the immediate vicinity. On the Mexican side of the fence is a cement-enforced canal with houses and quite a bit of light (RT 68-69).

Turner, in his unmarked car with a 5-foot police radio aerial (M RT 23-24), drove right past the two men, proceeded to the west end of International Street, turned around, drove past the men again, parked his car somewhat further east, and got out of his car in order to follow the men on foot (M RT 23). He followed them for about five blocks (M RT 9, RT 25) through a well lighted and residential area which also has government offices which are closed after 5:00 p.m. (RT 73-77); they were walking on the sidewalks in an average manner and were not carrying anything (RT 73-76).

Next, the two men entered a red Falcon Ranchero bearing California plates, and drove off (M RT 10). Turner lost surveillance for approximately half a minute (M RT 40-41) while he ran back to his own car, but then followed the Ranchero, which returned to the area near the fence (M RT 9). They stayed three or four minutes in the area near the fence during which time the Ranchero was not in his view (M RT 9). When the Ranchero returned there were three people in it (M RT 9). The Ranchero turned North on Hereford Street to Crawford to Sonoitta and back to International Street (M RT 9). Turner then proceeded north on Grand Avenue (M RT 10); Turner waited and saw the Ranchero go past approximately one mile north of the port, make a U-turn and stop in front of a Richfield Station headed south (M RT 10). It was not again seen until some 10-15 minutes, except when Agent Swindler, who was sent to pass the station, saw them still there (M RT 86). Swindler parked some distance away (M RT 86). When the car was seen headed north by the other agents, Turner, Washington and Cameron, Swind-

ler was sent to check the closed Richfield Station to see if they had left anything there, and found nothing; he so reported to the other agents (M RT 86).

Swindler caught up with the other agents who then at approximately twelve miles north of the port stopped the Ranchero (M RT 11). During this drive, the Ranchero would slow down and speed up as if looking for a tail; the officers waited until they were sure that the Ranchero wasn't going back to town, that they already had the contraband (M RT 11). All three men were in shirtsleeves when stopped (RT 34). A search that followed the stopping of the vehicle revealed ten and one-half pounds of marijuana in a bag under the hood (M RT 52; RT 30) and 115 benzedrine tablets wrapped in a wet olive drab jacket and a wet black sweater in the back of the Ranchero (M RT 52) and one tablet on the person of Cleaver (RT 33, 129), (as well as one tablet on Stewart's person (RT 129)). Cleaver had grimy hands (RT 95) and Turner in getting the bag out of the engine compartment got his hands greasy (RT 30).

### III.

#### **OPPOSITION TO SPECIFICATION OF ERRORS**

1. The search twelve miles north of the border was not sustained as a border search but was a search based on probable cause.
2. The information, coupled with the observations of the agents corroborating the informer's information and the Appellant's movements constituted probable cause.

## IV. ARGUMENT

**The search, based on information and the observations of the agents corroborating the information and the Appellant's movements, was a search based on probable cause.**

Appellant's counsel argues for some five pages that the search cannot be sustained as a border charge. Count I of the Indictment charged receiving, concealing, etc., not importation or smuggling. The Government in its Memorandum in Opposition to Appellant's Motion to Suppress or in the Alternative to Disclose Confidential Informant (RC, Item 4) alleged the search was based on probable cause and that no grounds had been asserted for revealing the informant, *Roviaro v. United States* (1957) 353 U.S. 53, 77 S.Ct. 623, 1 L.E. 2d 639, and therefore, the Government's privilege may be invoked, *McCray v. Illinois* (1967) 386 U.S. 300, 87 S.Ct. 1056, 18 L.E. 2d 62.

At the hearing on Appellant's Motion to Suppress Evidence, or in the Alternative to Disclose Name of Confidential Informant, Government's counsel stated the Government's search was not based on border search (M RT 4, L 16-23). Why Appellant's counsel still argues it was not Border search is not apparent to Appellee.

Title 19 U.S.C.A. §1461, does provide that a person entering the country must unload his baggage and unlock his vehicle, etc. However, 19 U.S.C.A. §482 provides that Government officers may both within or without their districts stop and search any vehicle in which he may have a reasonable cause to suspect there is merchandise which was imported contrary to law.

In *Bailey v. United States* (5th Cir., 1967) 386 F.2d 1 at pages 203, the Fifth Circuit held:

"As this was a warrantless search not incident to an arrest, the government either must have a finding that probable cause existed or must excuse its absence by resort to the border search doctrine. No case has held that one who has not crossed an international boundary can be the object of a constitutionally permissible border search, and we do not reach that question. Rather, we assume the view of the searching officers, and hold that 'the facts and circumstances within their knowledge and of which they had reasonably trustworthy information were sufficient in themselves to warrant a man of reasonable caution in the belief' that appellants were, when searched, possessed of illegal narcotics."

In *Sirimarco v. United States* (10th Cir., 1963) 315 F.2d 699, the Tenth Circuit held, under the statute providing for seizure of vehicles used to transport counterfeit bills, 49 U.S.C.A. §781 (3), that the agent had probable cause to transport counterfeit bills and that, since he had the right to seize the car, the search was lawful even though he did not first assert formal control over it.

Title 19 U.S.C.A. §1595a provides:

"(a) Except as specified in the proviso to section 1594 of this title, every vessel, vehicle, animal, aircraft, or other thing used in, to aid in, or to facilitate, by obtaining information or in any other way, the harboring, or subsequent transportation of any article which is being used or has been introduced, or attempted to be introduced, into the United States contrary to law, whether upon such vessel, vehicle, animal, aircraft, or other thing or otherwise, shall be seized and forfeited together with its tackle, apparel, furniture, harness or equipment."

The car was subject to seizure.

At the hearing on the Motion to Suppress, the Court asked Agent Turner the following:

"BY THE COURT:

"Q. This Nogales area, how would you describe the activity there with regard to bringing in or attempting to bring in narcotics, marijuana and so on and so forth?

"A This generally west fence area?

"Q The Nogales area, where you are stationed and where this activity took place.

"A There is a great deal of activity as to bringing in narcotics.

"Q Can you give me, say in the last year, can you give me in round figures approximately the number of arrests you have made of people, not you personally but the officers there at the Border?

"A Yes, sir. I believe the last fiscal year, to the best of my recollection, because it came up a while back, I believe two hundred arrests last year in connection with narcotic cases.

"Q How many of them are arrests where narcotics or contraband was found and prosecution was successful?

"A Of those two hundred cases, I would say prosecution was successful probably in eighty per cent.

"Q This man that got the information to you and whom you later contacted, he has been described as the informer. Have you had information from him prior to this time?

"A Yes, sir.

"Q Has this information been pursued?

"A Yes, sir.

"Q On occasion. Has it resulted in cases being made, arrests being made?

"A Yes, sir, it has.

"Q What percentage of the time have you found in the cases have you found his information to be accurate?

"A This particular informer, I would say around sixty.

"Q Sixty per cent?

"A Sixty per cent.

"Q Where you located these two men leaving or walking away from the fence, where is that with reference to the cemetery that has been described?

"A The only cemetery that I know of in relation to close to the fence, is about ten and a half miles west of the center of Nogales, the Grand Avenue Port of Entry, on the Mexican side, probably two to three hundred yards south of the International fence, almost immediately south of where the International fence ends, the chain link fence.

"Q Where was that in relation to where you saw these men?

"A That is about two miles west of where I saw these men.

"THE COURT: I believe that is all I have.

"MR. THIKOLL: Would the Court permit a few more questions? I didn't know the Court's position whether there would be any judicial notice taken of the activity at the Nogales Port of Entry. I haven't asked any questions on that subject.

"THE COURT: I am bound to take some notice of it inasmuch as I would say eighty per cent of my time in court now is devoted to narcotics arising in Nogales. I thought I would get it on the record with the witness, but I know these things actually from sitting here and hearing the cases." (M RT 70, L 23 to 73, L 5)

The Court found:

"THE COURT: You are forgetting Mr. Washington's testimony. When he was on the phone and talked to the informer and the informer said, "They have got a bag of grass and they have gone over the fence."

"MR. DAVIS:" (attorney for defendant Stewart) "I think the testimony is conflicting. One says they have a bag and the other says they have a bag of grass.

"THE COURT: It is two different conversations. It is a conversation with Mr. Washington and a conversation with Mr. Turner. Mr. Turner rushes back and said: 'Are you sure these guys went over the fence?' He said: 'Yes, they have a bag and went over the fence.' And without more he goes back. He doesn't say a bag of what. He has got the information that he wants and he leaves. This thing is done under a little bit of pressure, it isn't something that he can cross examine the informant about and still find the people you are looking for.

"MR. DAVIS: But then we go, Your Honor, to the description. We have a description of two OD jackets, whatever they were, whether they were fatigue or field, I don't think makes too much difference, two OD jackets and a black sweater. This is it. No description of the men, they could have been men eighty-five years old, could have been men fifteen years old. They could have been any description of this and I would venture to say that there are thousands of people, especially in Nogales, Arizona, wearing OD jackets. These are things that are bought in Army surplus.

"THE COURT: You can subdivide this thing beautifully, but are there thousands of people in Nogales where two of them would be wearing, one an OD jacket or a military jacket and one a black sweater and will be at a point by the fence where the informer has indicated in the middle of the night.

"MR. DAVIS: No one saw two men with OD jackets and a black sweater at a point —

"THE COURT: They saw one man with a military jacket and one man with a black sweater. That is two out of three. Then later on they went back to the very point from which they were walking and got the vehicle and went back, two of them went back and came out with a third.

"MR. DAVIS: But this third, the only evidence as to what this third was wearing is evidence that was obtained by the search and seizure at the time.

"THE COURT: That isn't important. You have two that meets the description and one isn't even there, but when they go back to the fence area, they come out with a third. Common sense would lead you to believe that they went back for this fellow, he stayed there for some reason, and a pretty good reason would be that he was going to be there with the stuff until they brought the vehicle back. I think you can of course subdivide a thing and resubdivide, but as the Draper case says and all the cases say, the ultimate question is whether the facts and circumstances within the knowledge of the agents, and this is all of the agents, not just one alone, but the agents as a whole, what they all knew together, whether on a basis of that they had reasonably trustworthy information that was sufficient to warrant them as men of reasonable caution in believing that the defendants were committing an offense, namely, that they were facilitating the transportation of marijuana. I think on the basis of the evidence, the fact that Mr. Turner gets a message from this informant he has had previous experience with and who on the basis of what he says about the information, I find to be a reliable informant, he gets the information that these men, describing their dress, their apparel, in Nogales and attempting to make a buy of marijuana. He goes immediately over to Mexico trying to locate the informant,

which he is unsuccessful, trying to locate the three men dressed as has been indicated and he is unsuccessful, but he gets a call from Mr. Washington who says: 'I have talked to the informant, the same reliable informant, and he tells me these fellows have bought marijuana and have gone over the fence, have jumped the fence.' With that Mr. Turner comes back to Arizona, he can't find the people where he thinks they ought to be, so he goes back, verifies with the informant that they have gone over the fence and have a bag at least, that is the expression. He goes again and he finds two people meeting the description of the informant, people that the informant has described to him, he keeps them under observation, sees them get into a Ranchero wagon, go back in the vicinity of the fence where they had come from, and when they come out they have a third person with them. Then from the testimony of the various agents, begins the procedure of going north, turning back, going north and turning back, driving slow, driving fast. As was described by one of the agents, conduct to indicate they were trying to find out if they were being pursued. In other words, conduct which would indicate a little bit of fear they might be involved in something they shouldn't and might be being observed.

"On the basis of all the evidence, I find that the information the officers had, the reasonably trustworthy information they had, it doesn't have to be one hundred per cent, just reasonably trustworthy information, at the time they stopped and searched the vehicle was sufficient in itself to warrant men of reasonable caution and belief, and the agents did believe that the defendants were committing the offense of facilitating the transportation of marijuana, and the Court concludes therefore the search was lawful."

(M RT 89, L 11 to 93, L 5)

Further, it is respectfully submitted, once the informant's information is corroborated by the agent's own observations, the informant need not be revealed to sustain the finding of probable cause. *Draper v. United States* (1959) 358 U.S. 307

at 313; 3 L.E. 2d 327, 79 S.Ct. 329; *Rocha v. United States* (9th Cir., 1967) 387 F.2d 1019 at page 1023; *Lemons v. United States* (9th Cir., dated February 28, 1968) No. 21,940, ..... F.2d ..... at page ..... (Page 4 of Slip Sheet Opinion).

Thus, with the information as to three men, two in O.D. Army jackets and one in a black sweater or jacket seen with Gradillas, a known narcotic dealer, who have gone over the fence with a bag of grass, and the agents see two men, one in a black sweater and one in an Olive Drab Army jacket walking from the brush onto International Street, in an area that is residential, going to a parked car, go back to the west end of International Street and return in 3 or 4 minutes with a third occupant, the information was corroborated. The car goes into a residential area, and then goes on to Grand Avenue which is the highway going north, makes a U-turn and stops, remains there about 10 or 15 minutes, drives north fast and then drives slow and fast again, as if checking for a tail, all of which constituted facts "sufficient in themselves to warrant a man of reasonable caution in the belief" that the car would contain "grass," i.e., marijuana.

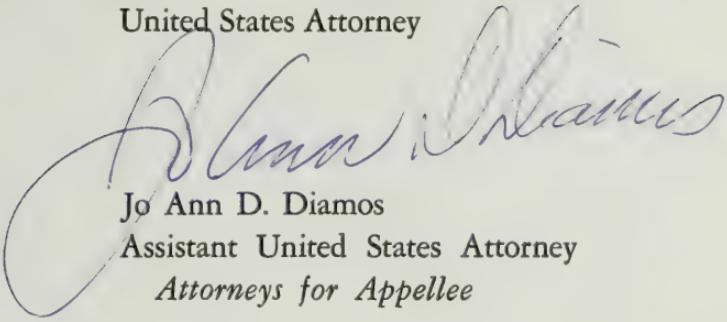
## V.

### **CONCLUSION**

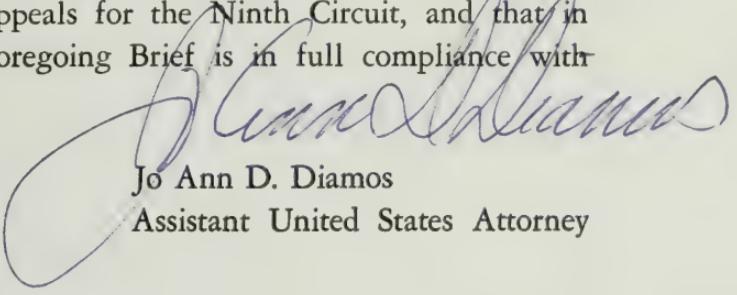
It is respectfully submitted the agents had probable cause to stop and search the vehicle and probable cause to believe the Appellant and the two other men were receiving, concealing, and facilitating the transportation and concealment of marijuana.

Respectfully submitted,

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I certify that, in connection with the preparation of this Brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing Brief is in full compliance with those rules.

  
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Three copies of the Brief of Appellee mailed this 1st day of May, 1968, to:

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SN 191968  
No. 22,593

IN THE

United States Court of Appeals  
For the Ninth Circuit

EDGAR HERBERT VICKERY,                                  *Appellant,*  
vs.  
FISHER GOVERNOR COMPANY,                                  *Appellee.*

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No. 22,593

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

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EDGAR HERBERT VICKERY,                                  *Appellant,*  
vs.  
FISHER GOVERNOR COMPANY,                                  *Appellee.*

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**BRIEF FOR APPELLEE**

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**I**

**JURISDICTIONAL STATEMENT**

Appellee (hereafter called "Fisher") accepts the jurisdictional statement set forth in the Brief for Appellant (hereafter called "Vickery").

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**II**

**STATEMENT OF THE CASE**

Since Vickery's Statement of the Case is not complete in several respects and contains irrelevant matter in many other respects, Fisher submits a concise abstract or statement of the case, as required by Rule 18.

#### A. The Pleadings

This action involves certain Royalty and Sales Agreements relating to ball valves (R. 7-34, reproduced as Appendices A and B respectively in Vickery's Brief). These Agreements were entered into between the parties in October, 1960 and were terminated by Fisher as of December, 1965 by written notice (R. 35) pursuant to Fisher's "unrestricted right to terminate this agreement at any time" (Paragraph 6 of the Royalty Agreement, R. 11).

The Amended Complaint alleges that Fisher's exercise of its unrestricted right of termination constituted a breach of the very Agreements which granted this right and, in addition, constituted a breach of a purported fiduciary obligation which Vickery alleges should be imposed upon the contractual obligations set forth by these Agreements. Vickery bases his allegations solely upon certain oral representations purportedly made by Fisher during the negotiations which preceded the preparation and execution of said Agreements.

Fisher's Answer denies any breach of contractual or fiduciary obligation and asserts that the termination was a proper exercise of the "unrestricted right" of termination expressly agreed to by both parties and specifically included in the Agreements at the time of their execution.

Fisher also has counterclaimed (a) for Declaratory Judgment that said Agreements were terminated as of December, 1965; (b) for Declaratory Judgment that Vickery did not have legal right and title to the

patent applications sold by Vickery to Fisher in that Vickery was not "the original, first and sole inventor" thereof as he had represented under oath to the Patent Office; and (c) for judgment dismissing the Amended Complaint for unclean hands due to Vickery's fraudulent and inequitable conduct in connection with the subject matter of the Agreements here in issue.

Only the right of Fisher to terminate the Agreements under the unrestricted termination provision is involved in the Summary Judgment here under appeal, the District Court having expressly directed that such judgment be entered in favor of Fisher with respect to Vickery's First Amended Complaint (R. 391).

#### **B. History of the Agreements in Suit**

Fisher is a long established manufacturer and distributor of a wide variety of valves, actuators and other related devices used to control gas and liquid flow in many different applications. Prior to the Agreements here in suit, Vickery marketed certain valves primarily adapted for military or governmental end use. He had represented to Fisher that he had developed various types of ball valves and related actuators and devices, upon which he had filed several patent applications and that he possessed wide technical knowledge, experience and creative ability.

In 1960, Vickery and Fisher entered into certain negotiations which ultimately culminated in the Royalty and Sales Agreements here involved. These

Agreements, as finally executed, were the joint and considered results of numerous conferences, negotiations and bargaining between the respective parties and their counsel. In its opinion of July 19, 1967, the District Court held that Vickery was "an independent contractor who has dealt at arm's length, in entering into this agreement, and I don't think there is any dispute about this, by negotiations with the defendant, with both parties having a lawyer represent them" (T. 76). Various proposals and counter-proposals of course were made during such negotiations but all of the terms finally agreed upon by the parties were expressly embodied in the Agreements as executed.

Vickery's Amended Complaint admits (R. 155) that during the negotiations Fisher insisted that it have the "unrestricted right to terminate the Agreements at any time" during the life thereof, and this requirement was unequivocally set forth in Paragraph 6 of the Royalty Agreement, as follows:

Fisher has the unrestricted right to terminate this agreement at any time giving Vickery at least sixty (60) days prior written notice by U. S. Registered Mail addressed to Vickery at his last known address . . .

Vickery further has admitted that there is no other writing or document, executed by either party, which amends said Agreements, and that Fisher's written notice of termination, dated October 2, 1965, fully complied with all of the procedural requirements for termination set forth in the Agreements (R. 326).

**C. Fisher's Exercise of Its Right to Terminate**

In the Royalty Agreement, Vickery agreed to sell Fisher his ball valve developments and patent rights (Vickery brief, App. A, p. 2) to provide technical assistance and continuing development of improvements and additional inventions and to keep from competing with Fisher in the development and marketing of ball valves until Fisher exercised its right to terminate (Vickery brief, App. A, p. 5). Fisher agreed to pay an initial sum plus royalties and commissions up to a maximum period of ten years subject, however, to Fisher's unrestricted right to terminate the Agreement at any time (Vickery brief, App. A, p. 5). While the Agreement expressly did not limit Fisher's "unrestricted right to terminate", it did provide for different consequences depending upon whether Fisher elected to terminate either during or after an initial five year period.

**Termination Within  
First Five Years**

- (1) Fisher has to return all physical devices and materials
- (2) Fisher has to return all patents and applications assigned by plaintiff
- (3) Fisher has to terminate manufacture and sale
- (4) Fisher loses benefit of continuing Vickery assistance, development and inventions
- (5) Vickery can compete with Fisher in the development and marketing of ball valves

**Termination After  
First Five Years**

- (1) Fisher retains ownership of all physical devices and materials
- (2) Fisher retains ownership of all patents and applications assigned by plaintiff
- (3) Fisher may continue manufacture and sale
- (4) Fisher loses benefit of continuing Vickery assistance, development and inventions
- (5) Vickery can compete with Fisher in the development and marketing of ball valves

In its Order of December 18, 1967, the lower Court held that "*the contract is unambiguous in that unrestricted right of termination means exactly what it says*" (R. 483) (Emphasis added). The option to terminate the contract either during or after the initial five year period was expressly intended to provide Fisher with an important business alternative, namely, whether the benefits of Vickery's non-competition restriction and his continuing technical contributions would economically justify the amount of royalties which would have to be paid for such benefits during the second five year period.

During the first five years of the Agreement, Fisher paid Vickery approximately \$750,000.00 in full compliance with the royalty and sales commission provisions of the Agreements (R. 327). If Vickery had continued to make inventive contributions sufficient to warrant continued royalty payments, Fisher could have elected to keep the Agreements in force for the second five year period. Here, Fisher elected to give up the benefit of obtaining any continuing assistance, development and inventions from Vickery by exercising its unrestricted right of termination. All of these acts were in admitted accord with the express terms and conditions of the Royalty Agreement and cannot constitute any breach thereof.

As the District Court pointed out most explicitly in its opinion of July 19, 1967 (T. p. 76):

"The Court: And I would include in the ruling that there has been no breach of any fiduciary relationship, because the defendant had

the right under the existing contract to terminate and did terminate them lawfully and rightfully under the language of Exhibits A and B . . . (if) they have a right to terminate it, I don't see any breach of anything, including any fiduciary relationship."

#### **D. The Rulings of the District Court**

Vickery has appealed from the Order of August 14, 1967 granting Summary Judgment and from the Order of December 18, 1967 denying Vickery's motions to set aside the Summary Judgment Order; for leave to amend the First Amended Complaint to add a new cause of action for reformation thereto, and to set aside the Pretrial Order filed on March 10, 1967.

For the convenience of this Court, the Order of August 14, 1967 (R. 390) has been reproduced as Appendix A herein and the Order of December 18, 1967 (R. 482) has been reproduced as Appendix B herein. An extract of the proceedings of July 19, 1967 covering the trial court's ruling in support of the Summary Judgment is reproduced herein as Appendix C.

#### **E. The Questions on Appeal**

The questions on appeal may be stated quite simply as follows:

1. Whether the lower Court was correct in holding that there is no genuine issue of material fact to bar the grant of Summary Judgment and that as a matter of law Fisher properly terminated and did not

breach the Royalty and Sales Agreements upon which the Amended Complaint is based; and

2. Whether the lower Court was correct in denying Vickery's belated motion filed after trial, to amend his First Amended Complaint to add a new cause of action for reformation of the Agreement for the reasons that said motion was unduly dilatory, that Fisher would be prejudiced thereby and that such amendment, if allowed, would be subject to a motion to dismiss as lacking any legal basis for reformatory relief.

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### III ARGUMENT

#### A. AN "UNRESTRICTED" RIGHT TO TERMINATE MEANS EXACTLY WHAT IT SAYS

1. An unrestricted right of termination was a specific bargaining issue which Fisher insisted on as a condition to finalizing the contract.

The District Court's construction of the contracts in issue so as to give effect to Fisher's "unrestricted right of termination" was inescapable in the light of the plain, simple import of the language used by the parties themselves after vigorous debate, negotiations and bargaining over this precise point.

A number of proposed drafts of the agreement were exchanged between the parties (see plaintiff's declaration and preliminary drafts attached thereto beginning at R. 421) before the contract was finally executed. As the District Court noted in this connection,

Fisher refused to accept a contract which did not include an unconditional right of termination:

"In fact, plaintiff's counsel submitted a proposed contract to defendant which excluded the right to terminate during the second five years of the contract. Defendant refused to accept this draft and plaintiff, knowing that he (plaintiff) was giving defendant an unrestricted right to terminate, signed the agreement." (R. 484)

The language of the final Agreement between the parties is quite clear:

"6. Fisher has the unrestricted right to terminate this agreement at any time . . . if Fisher exercises its right of termination . . . both parties shall have released from all further obligations . . ." (Vickery's brief, Appendix, p. 5)

Moreover, Vickery concedes that the right of termination was a crucial consideration. In Par. IV of the First Amended Complaint, Vickery alleges:

"(Fisher) *insisted* that Fisher have the right to terminate the . . . agreements at any time . . ." (R. 155, emphasis added)

After considering the various affidavits, declarations and preliminary drafts, the District Court likewise noted that Fisher's right of termination went to the essence of the contract.

"Plaintiff . . . knew that the Defendant *insisted* on the right-to-terminate clause" (R. 484, emphasis added).

In addition to the specific termination procedure in Paragraph 6 of the Agreement, quoted above, there

are numerous other references throughout the Agreements to Fisher's right of termination:

"(Subject) to termination prior to the end of said period as hereinafter set forth . . ." (Par. 3 Royalty Agreement, Vickery's brief, Appendix, p. 3)

"7. In the event Fisher *exercises* the right of termination . . ." (*ibid.*, Appendix, p. 6)

"8. In the event of the termination of this agreement . . ." (*ibid.*, Appendix, p. 6)

"11. . . . (If) after Vickery's death, Fisher elects to exercise the right to terminate this agreement . . ." (*ibid.*, Appendix, p. 8)

The Sales Agreement likewise contains language referring to a termination of the Royalty Agreement.

"7. . . . (In) the event of cancellation of the aforesaid royalty agreement between the parties, this Agreement shall be cancelled automatically." (*ibid.*, Appendix, p. 16)

The District Court, having fully considered all of the pleadings and exhibits thereto, together with the pretrial order, various stipulations, declarations, affidavits, and memoranda (R. 390) *concluded most emphatically*:

- (1) "that the contract clearly expresses the real intention of the parties . . ." (R. 484) and
- (2) "that the contract is unambiguous in that 'unrestricted right of termination' means exactly what it says. Thus, parol evidence cannot be introduced to change that language . . ." (R. 483)

2. Plaintiff's self-serving efforts to engraf on the plain language of the termination clause any unilateral limitations are precluded by both the doctrine of merger as well as the parol evidence rule.

Admittedly a great deal of negotiations, conferences, and bargaining preceded the final draft of the Royalty Agreement as executed by the respective parties. In the absence of mistake or fraud, all such preliminary negotiations and representations become merged into the actual written agreement (see *Murphy v. Continental Insurance Co.*, 178 Iowa 375, 157 N.W. 855; 17 Am. Jur. 2d, Contracts, 260). Where the written contract is a self-contained, integrated agreement, it is presumed to contain all the terms and conditions agreed to by the parties (see *McKenney and Seabury v. Nelson*, 220 Iowa 504, 262 N.W. 101; *Security Savings v. Capp.*, 193 Iowa 278, 186 N.W. 927). Evidence of preliminary conversations by the parties is inadmissible since they are deemed to be superseded by the final written agreement (*Corklin v. Silver*, 187 Iowa 819, 174 N.W. 573; *Indianapolis Terra-Cotta Co. v. Murphy*, 99 Iowa 633, 68 N.W. 898).

As the District Court also noted above, in the absence of ambiguity, parol evidence likewise is inadmissible to vary or alter the written terms of a contract. (*Gordon v. Witthauer*, 138 N.W.2d 918 (Iowa); *Schnabel v. Vaughn*, 140 N.W.2d 168 (Iowa).) Moreover, even where parol evidence is admissible, its use is restricted to resolving an ambiguity (*Conrad Milwaukee Corp. v. Wasilewski*, 141 N.W.2d 240 (Wisc.) and not to alter or contradict a specific term or pro-

vision in the written contract (*Crompton-Richmond Co. Inc. v. Smith*, 253 F.Supp. 980 (E.D. Penn. 1966)). This rule is stated very explicitly by the court in the case of *Aultman v. Meyers*, 33 N.W.2d 400, 239 Iowa 940, which also is cited in Vickery's brief p. 36, in noting that "parol evidence does not change or contradict the wording of the instrument, but only explains, clarifies or removes any doubts as to its meaning." The parol evidence rule under Iowa law is one of substantive law and not merely evidentiary (*Rasmus v. A. O. Smith Corp.*, 158 F.Supp. 70 (N.D. Iowa)).

It therefore is submitted that there is no ambiguity in the Agreement, that all preliminary negotiations are merged in the final written document, and that in any event, parol evidence can be used only to resolve, and not to contradict, the express provisions of a contract.

3. **Fisher's right of termination did not exist in a vacuum but imposed consequences clearly spelled out in the contract and involved substantial economic-business considerations.**

Parties to a contract typically provide a method of termination which the Courts enforce in accordance with the plain meaning of the language used (*Shain v. Washington National Insurance Co.* (8 Cir.), 308 F.2d 611; *Republic Coal Co. v. W. G. Block Co.* (Iowa), 190 N.W. 530; 17A C.J.S., Contracts, Secs. 396, 399; 12 Am. Jur., Contracts, Sec. 434), and irrespective of the reasons or motives of the party exercising the right (*American Machine v. DeBothezal*, C.A.2, 180 F.2d 342; *Green Bay Auto Inc. v. Willys*,

102 F.Supp. 151; *Rubinger v. I.T.&T.*, 193 F.Supp. 711; 17A C.J.S., Contracts, Sec. 399; see also 45 Harvard Law Review 378).

Notwithstanding the prerogative of private parties to bargain over the terms and conditions of a mutual agreement, it is respectfully submitted that Fisher did not merely have a "unilateral option to pay or not to pay" as suggested by Vickery (see Vickery brief, p. 30, Sec. 3). On the contrary, as a result of exercising its right of termination, Fisher had to surrender or give up valuable economic benefits in accordance with a formula laid out very explicitly in the contract:

"7. In the event Fisher exercises the right of termination prior to October 1, 1965 (note that the contract became effective October 1, 1960), then and in such event Fisher shall be obligated to:

transfer to Vickery, promptly after the date of termination, all of Fisher's right, title and interest in and to *all physical property* delivered to Fisher pursuant to Paragraph 1.3 which then is in existence, together with all designs and data in its possession relating to ball valves, free and clear of any interest of any third party and to deliver the same to Vickery; and

assign and deliver to Vickery, promptly after the date of termination, *all patent applications* and patents which may have been issued thereon which (i) are assigned to Fisher pursuant hereto and (ii) may be assigned to Fisher pursuant to the terms hereof; and

forthwith permanently *cease the production* and sale of any of the products specified in the

above Paragraphs, except such products as Fisher may have in inventory on hand at the date of termination."

In addition to the physical products enumerated above, the Court also will note that Fisher, in effect, was purchasing not merely patents per se but also Vickery's technical skill, which was covered twofold, one by an affirmative duty to provide continuing consultation and invention services, and negatively by a noncompetition provision during the lifetime of the contract (Appendix, Royalty Agreement, Par. 5).

The exercise of Fisher's "unrestricted right of termination" therefore created an important business alternative. In the event the contract was terminated prior to the expiration of an initial five-year period, Fisher had to return various physical properties and patent rights. On the other hand, if the contract were terminated after the initial five-year period, Fisher lost the benefit of what Paragraph II of the First Amended Complaint describes as Vickery's "highly technical" engineering skills (R. 154). In its exercise of the termination provision, Fisher therefore had to elect whether Vickery's continuing technical contributions, if any, economically justified the amount of royalties which would have to be paid as consideration for his future services.

A secondary thrust in the Vickery brief, in an effort to avoid the plain meaning of Fisher's right of termination, is an argument (beginning at p. 33) to the effect that the Court should impose a judicial limitation on what would otherwise constitute an "un-

restricted right". The cases which Vickery cites for this proposition, however (1) fail to support such a principle; (2) involve different contractual provisions and (3) arise out of different factual settings.

In *Richard Bruce Co. v. J. Simpson & Co.*, 243 N.Y.S.2d 503, a contract gave an underwriter "absolute discretion to terminate" if the underwriter determined that market conditions . . . etc. The Court held that the underwriter's determination of whether market conditions were favorable, had to be reasonable and not arbitrary.

In *Dubois v. Gentry*, 184 S.W.2d 369, a lease provided for termination by the lessee "for any reason" other than wilful refusal to abide by it. . . . The Court accordingly held that the lessee's option was in effect limited and could only be exercised on a showing of reasonable grounds.

In the case of *Quick v. Southern Churchman Co.*, 199 S.E. 489, 171 Va. 403, the parties had a bilateral "right of termination" for just cause, which the Court again construed as requiring some showing of reasonable grounds and not mere whim.

The cases above cited are accordingly clearly distinguishable from the case at bar, in that they all have express contractual limitations on the exercise of a right of termination. The instant case, on the other hand, achieves essentially the same results by expressly spelling out the contractual results or effects of the exercise of such a power, so that its exercise is not capricious or unilateral, but instead imposes

substantial economic consequences in accordance with a formula agreed to by the parties.

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#### B. THERE WAS NO FIDUCIARY DUTY

Vickery urges that the circumstances of the parties resulted in a fiduciary and confidential relationship between them and that Fisher breached obligations imposed by the law under that relationship when it exercised its contractual right to terminate the Agreements. No case cited by him, however, discloses factual situations comparable to the facts in the instant case.

In neither *Stevens v. Marco*, 147 C.A.2d 357, 305 P.2d 669 (1956), nor *Saco-Lowell Shops v. Reynolds*, 141 F.2d 587 (4 Cir. 1944), did the defendant terminate the arrangement between the parties under an express right given in the contract. Furthermore, in the *Stevens* case, a release executed by the plaintiff was obtained by the defendant (an attorney who had undertaken to prosecute plaintiff's patent application) after falsely representing to plaintiff that no patent was going to issue. The Court held that his false representation made the release invalid from its inception and the plaintiff was not bound thereby.

In the case of *Baker Oil Tools v. Burch*, 71 F.2d 31 (10 Cir. 1934), the arrangement between the parties was not entirely set forth in the written contract, and there were collateral undertakings not covered by the writing nor referred to therein. In the course of its opinion, the Court observed, "If this suit were on the

license agreement alone, as Baker contends, the preliminary negotiations would be merged into it and evidence thereof immaterial."

It is clear that Fisher entered into the Agreements in good faith, that it abided by all the terms and conditions of the Agreements while the same were in effect, including the payment to Vickery of \$200,000.00 under the Royalty Agreement and some \$525,000.00 under the Sales Agreement (R. 327), and that it exercised a right expressly given and paid for when it terminated the Agreements. The law requires nothing more than that a party live up to the terms of its contract and here Fisher has clearly done so. Vickery's position that a party can breach a contract or any kind of a fiduciary duty by exercising an unrestricted right expressly reserved to it under the contract is a wholly untenable one. Certainly, the cases cited by Vickery do not stand for such an unsettling proposition which would completely confuse otherwise orderly contractual arrangements.

It is important to bear in mind that Vickery was an independent contractor, that both parties were represented by able counsel throughout the contract negotiations, that the arrangement between the parties related to the *sale* of patent applications and related items of personality and did not constitute a licensor-licensee relationship, and during the initial five-year existence of the contracts, Fisher paid over \$750,000.00 to Vickery while at the same time investing over \$1,000,000.00 in plant and equipment to develop the ball valve program. These facts are quite unlike the facts in the cases cited by Vickery

to support his position in this case. Here, no dollar investment was made by Vickery in setting up the Fisher facilities with which to carry on the ball valve business. Here, there was no franchise arrangement or licensor/licensee relationship where the licensor has retained title to the patents and the licensee is exploiting them, as in *Hyde Corporation v. Huffines*, 158 Tex. 566, 314 S.W.2d 763, cited by Vickery.

To the contrary, the instant case concerns the outright sale to Fisher of the patent applications for a valuable consideration and under circumstances where Fisher (not Vickery) was required to invest substantial sums of money to make the program commercially feasible. This case is simply not like the *Hyde* case nor the automobile dealer cases which have resulted in the finding of a fiduciary obligation (see remarks of the District Court, brief App. C, p. xiii).

Nor is it like *Winn v. Rudy Patrick Seed Co.*, 249 Iowa 431, 86 N.W.2d 678, where the defendant advanced funds to the plaintiff to cover the cost of seed to be purchased on the market by plaintiff. The issue in that case was whether an acceptance of a final settlement check by plaintiff constituted an accord and satisfaction and precluded any further accounting between the parties. The Court held that an accord and satisfaction existed in spite of claims by plaintiff that defendant engaged in intentional and fraudulent misrepresentations in inducing acceptance of the settlement check.

In *Lukens Steel v. American Locomotive Company* (N.D. N.Y.) 99 F. Supp. 442, the Court observes that

the relationship did *not* involve "arm's length" dealing (cf. finding of the District Court that Vickery was an independent contractor dealing at arm's length (brief App. C, p. xiii)). Here again, the *Lukens* case is one that involves bad conduct at the beginning of the relationship, and therefore it manifestly is different from the facts of the case at bar.

Accordingly, it is submitted that the authorities relied upon by Vickery are inappropriate to support his contentions under the facts of this case. The Agreements particularly and explicitly defined the relationship and obligations of the parties. No other obligations should be or were intended to be superimposed upon or added to the plain words of the contract. Fisher's lawful exercise of an unrestricted termination right expressly granted to it by Vickery simply does not give rise to any breach of contract or breach of fiduciary duty action. Since this is solely a matter of law and there are not material questions of fact on this point, the ruling of the District Court should be sustained.

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**C. THE DISTRICT COURT PROPERLY DENIED VICKERY'S MOTION, MADE AFTER TRIAL, TO ADD A NEW CAUSE OF ACTION TO THE AMENDED COMPLAINT**

Vickery filed his initial Complaint on October 22, 1965 charging only breach of contract (R. 1). Both parties engaged in extensive discovery proceedings, including the taking of depositions in California, Iowa and North Carolina. Hundreds of documents were produced, inspected and copied.

On September 19, 1966 following such discovery, Vickery filed his First Amended Complaint for Damages, again grounded only on alleged breach of contract (R. 153). After substantial trial preparation and the submission of extensive pretrial statements, this cause went to trial on July 19, 1967. At the trial, Fisher moved for a summary judgment that the Agreements in suit had properly been terminated pursuant to their express terms, and the District Court, after fully considering the documents on file and the oral arguments of counsel, directed that summary judgment be entered for Fisher with respect to Vickery's First Amended Complaint for Damages (R. 390).

On August 23, 1967, over one month after the trial, Vickery belatedly moved for leave to file a Second Amended Complaint for Damages which included, *for the first time in this case*, a new cause of action asking reformation of the Royalty Agreement because of alleged "mutual mistake of the parties" (R. 392-407). Vickery concedes that the alleged facts upon which this new cause of action is based were known to Vickery at the time he filed his original Complaint in 1965 (R. 421-425). This new cause of action accordingly could have been included in the original Complaint, or even in the First Amended Complaint, but it was not until after Vickery received an adverse ruling at the trial that he chose to urge this new theory of reformation.

Significantly, no explanation, excuse or justification for his undue delay has been offered by Vickery.

Vickery has been represented by the same counsel since the initial negotiations with Fisher, since the execution of the Agreements in question and during this entire lawsuit. It is noted that Vickery's belated motion to amend was not supported by any affidavit of Vickery or his counsel attempting to justify Vickery's dilatory tactics in moving to amend the Complaint after trial.

Under Rule 15(a), F.R.C.P., leave to amend should freely be given if justice so requires. This does not mean under any and all conditions, and the courts have refused amendment of a pleading where undue delay or prejudice will result from such amendment.

In *Foreman v. Davis*, 371 U.S. 178 (1962), the Supreme Court stated that leave to amend should be granted only "in the absence of any apparent or declared reason—such as undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment, etc. . . ."

In this case, not just one, but practically all of the above reasons were present to justify the District Court's denial of the motion.

Vickery's delay was undue because the cause of action for reformation could have been pleaded in the original Complaint filed two years before the motion to amend. However, Vickery did not do so and no substantive reasons have been given for his dilatory tactics.

Further, Vickery could have cured the alleged omission by asserting the new cause of action in his First Amended Complaint, but again he did not do so—and again no excuse has been given.

Still further, the allowance of the amendment would have resulted in undue prejudice to Fisher who had believed its lengthy and expensive trial preparation to be completed, based upon the issues raised by the original and First Amended Complaints. It is noted that Vickery's declaration in support of his motion relies upon certain purported statements made by one Paul Elfers, a former employee of Fisher (R. 422). Although Vickery took lengthy and extensive discovery depositions of Fisher's present and former employees, no deposition was taken of Mr. Elfers. If the motion had been granted it would have necessitated the reopening of discovery for one or more depositions. In addition, new motions, pretrial statements, pleadings and trial preparation would have been required with respect to the new issues raised by the proposed new cause of action.

In *Hancock Oil Co. v. Universal Oil Products Co.*, 129 F.2d 959 (9 Cir. 1941), a patent case, defendant sought to amend its Answer more than two years after it was filed. The District Court's decision denying the proposed amendment for undue delay was affirmed by the Ninth Circuit Court of Appeals.

Similarly, the undue delay in *C. E. Stevens v. Foster & Kleiser Co.*, 109 F.2d 764 (9 Cir. 1940), was the basis for the Court's denial of leave to amend. The Court considered that "the long attention of

eminent counsel on both sides" in the case was sufficient to sustain a summary judgment and deny a motion for leave to amend.

In *Caddy-Imber Creations, Inc. v. Caddy*, 299 F.2d 79 (9 Cir. 1962), a copyright case having facts similar to the present case, the Court denied leave to amend where, after the evidence was in, appellant for the first time urged new legal theories involving an express contract and a contract implied in law. The Ninth Circuit affirmed the District Court's action in denying leave to amend the pleadings to add new theories because of movant's undue delay and the prejudice which would have resulted from such a belated amendment.

Directly in point is *Inland Steel Products v. M.P.H. Manufacturing Corp.*, 25 F.R.D. 236 (D.C. Ill. 1959), a patent case where the Court denied leave to amend the Answer several years after the Complaint was filed, after extensive discovery had been taken and where there was "no showing of oversight, inadvertance, or excusable neglect to account for the long delay."

To support his argument that the District Court should have granted the belated motion to add a new cause of action, Vickery's brief urges several grounds —each of which is wholly unsupported by the facts and each of which is directly contrary to the District Court's findings.

For example, Vickery argues that he cannot be charged with delay (Vickery brief, p. 38). This is wholly contradicted by the Court's findings that Vick-

ery "has known the facts upon which he proposes to base his amendment from the outset of this action and thus has been derelict in not offering the amendment long before Summary Judgment was entered against him" (R. 483).

Vickery also argues that Fisher will not be prejudiced by the addition of the proposed reformation count (Vickery brief, pp. 38, 39). On the contrary, the Court found that Fisher "having done all his work in preparation for trial, stands to be prejudiced by the amendment in that he will be forced to re-prepare on a new theory of liability not heretofore brought to his attention" (R. 483).

Finally, Vickery argues that the proposed new count is needed to enable him to show that "by mutual mistake of the parties" the Agreements did not completely and accurately reflect their understanding (Vickery brief, p. 37). The Court correctly ruled that it would be a futility to permit the amendment for this purpose since the alleged cause of action pleaded therein could not be legally sustained. The carefully reasoned opinion of the Court holds (R. 483, 484) :

"Finally, were the plaintiff allowed to amend the complaint to set forth the count in reformation, such count would be subject to a motion to dismiss as the facts alleged therein do not show mistake, fraud, or inadvertence. On the contrary, it is uncontradicted in affidavits and pleadings demonstrate that the contract clearly expresses the real intention of the parties. Plaintiff (who was at all relevant times represented by very able counsel) knew that the defendant insisted on the

right to terminate clause. In fact, plaintiff's counsel submitted a proposed contract to defendant which excluded the right to terminate during the second five years of the contract. Defendant refused to accept this draft and plaintiff, knowing that he (plaintiff) was giving defendant an unrestricted right to terminate, signed the agreement.

'A Court of equity will not reform a contract when all of the parties thereto acted with full knowledge of an omission before signing. It is only when stipulations which the parties *intended to express* have been omitted by mistake or through fraud.' (sic) (emphasis added) *Graves v. Greenfiel*, 196 Iowa 696, 195 N.W. 253 (1923).

In the case at bar, the allegedly omitted portions of the contract were omitted by design rather than by mistake, fraud, or inadvertance. Thus, there is presented in the proposed amendment, no ground for reformatory relief."

It is manifest that Vickery is wholly unable to show any valid legal reason for again amending his Complaint to add a new cause of action two years after the filing of the lawsuit, and after completion of discovery and the granting of summary judgment at the trial. The District Court's denial of the motion to amend was clearly proper and necessary under the circumstances.

## IV

**CONCLUSION**

For the reasons stated above, it is respectfully submitted:

That this Court should affirm the Order Granting a Summary Judgment in favor of Defendant entered on August 14, 1967, as well as the Order Denying Plaintiff leave to file an Amended Complaint adding a new cause of action for reformation, said Order being made on December 18, 1967, upon the grounds that appellant has failed to sustain the burden of showing error as required by Rule 52, Federal Rules of Civil Procedure.

Dated, June 11, 1968.

PELTON & GUNTHER,  
By THOMAS N. KEARNEY,  
BAIR, FREEMAN & MOLINARE,  
By SHELDON WITCOFF,  
CARTWRIGHT, DRUKER, RYDEN & FAGG,  
By REX J. RYDEN,  
*Attorneys for Appellee.*

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

THOMAS N. KEARNEY,  
*Attorney for Appellee.*

(Appendices A, B and C Follow)



## **Appendices A, B and C**



## **Appendix A**

---

United States District Court,  
Northern District of California

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Civil Action No. 44,301

---

Edgar Herbert Vickery,                                  Plaintiff,  
  }  
vs.  
Fisher Governor Company,  
an Iowa corporation,                                  Defendant.

---

### **ORDER GRANTING MOTION FOR SUMMARY JUDGMENT**

The above-entitled action having come on regularly for trial on July 19, 1967; and

The Court having considered all of the pleadings and exhibits thereto, together with the pre-trial order and all of the stipulations, admissions, declarations, affidavits, pre-trial statements and memoranda of points and authorities on file herein; and

The Defendant having renewed a motion for summary judgment previously made by Defendant, pursuant to Rule 56, Federal Rules of Civil Procedure, on the ground that as a matter of law Defendant properly terminated and did not breach the Royalty and Sales Agreements on which Plaintiff's amended complaint is based; and

The Court having heard oral argument of counsel on said renewed motion in open court at the time of trial; and

The Court having considered the matter and expressed the basis for its decision in open court.

The Court now expressly determines that there is no genuine issue of material fact with respect to the subject matter of said motion, except as to the matter of the amount of commissions due and unpaid by Defendant to Plaintiff pursuant to the terms of Subparagraphs (C) and (D) of Paragraph 5 of said Sales Agreement, which amount, by the approval of the form of this order, the parties have agreed is \$1,439.31 and which amount Defendant has agreed to pay to Plaintiff forthwith; and

The Court now expressly determines that there is no just reason for delay, it therefore is

ORDERED that said motion be and the same hereby is granted, and it is expressly directed that judgment be entered herein in favor of Defendant with respect to Plaintiff's First Amended Complaint for Damages.

Made on July 19, 1967 and presented for signature on August ..., 1967.

---

United States District Judge

Approved as to form:

Pelton & Gunther

By.....

Attorneys for Defendant

Edward K. Allison

Attorney for Plaintiff

## Appendix B

United States District Court,  
Northern District of California

Civil Action No. 44,301

Edgar Herbert Vickery, Plaintiff,  
vs.  
Fisher Governor Company, an Iowa corporation, Defendant.

### ORDER

It Is Ordered that the Motion of the plaintiff to set aside the order granting motion for summary judgment and the judgment entered pursuant thereto on August 14, 1967 and to grant plaintiff a new trial pursuant to Rule 59(a) of Federal Rules of Civil Procedure, having been submitted and the Court having duly considered the same, is DENIED.

It Is Further Ordered that motion of the plaintiff to vacate the order granting motion for summary judgment and the judgment entered pursuant thereto on August 14, 1967 pursuant to Rule 59(e) of Federal Rules of Civil Procedure, having been submitted and the Court having duly considered the same, is DENIED.

It Is Further Ordered that the motion of the plaintiff for leave, pursuant to Rule 15(a) Federal Rules of Civil Procedure, to amend his First Amended Complaint for damages to add a second cause of action thereto for reformation of said agreement, having been submitted and the Court having duly considered the same, is **DENIED** for the following reasons:

1. The affidavits on file, along with the memorandum and pleadings, afford ample proof to the effect that plaintiff has known the facts upon which he proposes to base his amendment from the outset of this action and thus has been derelict in not offering the amendment long before summary judgment was entered against him.
2. Defendant, having done all his work in preparation for trial, stands to be prejudiced by the amendment in that he will be forced to re-prepare on a new theory of liability not heretofore brought to his attention.
3. More important, the contract is unambiguous in that "unrestricted right of termination" means exactly what it says. Thus, parole evidence cannot be introduced to change that language. The very basis upon which the plaintiff seeks to amend his complaint is supportable only by that parole evidence which may not be introduced to alter the agreement.
4. Finally, were the plaintiff allowed to amend the complaint to set forth the count in reformation, such count would be subject to a motion to dismiss as the facts alleged therein do not show mistake, fraud, or inadvertence. On the contrary, it is uncontradicted in

affidavits and pleadings demonstrate that the contract clearly expresses the real intention of the parties. Plaintiff (who was at all relevant times represented by very able counsel) knew that the defendant insisted on the right to terminate clause. In fact, plaintiff's counsel submitted a proposed contract to defendant which excluded the right to terminate during the second five years of the contract. Defendant refused to accept this draft and plaintiff, knowing that he (plaintiff) was giving defendant an unrestricted right to terminate, signed the agreement.

"A court of equity will not reform a contract when all of the parties thereto acted with full knowledge of an omission before signing. It is only when stipulations which the parties *intended to express* have been omitted by mistake or through fraud." (sic) (emphasis added) *Graves v. Greenfield*, 196 Iowa 696, 195 N.W. 253 (1923).

In the case at bar, the allegedly omitted portions of the contract were omitted by design rather than by mistake, fraud, or inadvertence. Thus, there is presented in the proposed amendment, no ground for reformatory relief.

It Is Further Ordered that plaintiff's motion for an order setting aside the pretrial order filed herein on March 10, 1967 is denied.

Dated this 15th day of December, 1967.

/s/ C. A. Muecke  
U. S. District Judge

Original Filed Dec 18 1967  
Clerk, U. S. Dist. Court  
San Francisco

## Appendix C

### AN EXTRACT OF THE PROCEEDINGS OF JULY 19, 1967 COVERING THE TRIAL COURT'S RULING IN SUPPORT OF THE SUMMARY JUDGMENT

(T. pp. 67-77):

The Court: All right.

Well, gentlemen, I did do a lot of additional reading, and I also again very carefully went over the two agreements which are both stipulated to as being the agreements that pertain to this case, as far as any written agreements are concerned; I don't think there is any question about foundation, or anything of that sort, one pertaining to the Royalty Agreement, which is labelled Exhibit A to Complaint, and the other—Is that Exhibit B?

Mr. Allison: Yes, sir.

The Court: Yes. Exhibit B to the Complaint, pertaining to the Sales Agreement.

And I must say, first of all, I don't find any ambiguity in either of the agreements, and I will proceed and say why, for the record.

I find, for example, on page 3 of Exhibit A, which I have just referred to, being a royalty agreement, the words on the top of the first, not full paragraph, but the first full paragraph on the top of page 3, the 5th line, where it says, "subject to termination prior to the end of said period as hereinafter set forth," which again is a reference to the way in which the contract can be terminated.

In other words, modifying the full ten-year period.

Then there are three little paragraphs setting forth the royalties, and then again it refers to what would happen during the first five years, which I think

counsel for the plaintiff referred to, on the payment of not less than \$20,000 royalties a year, and "thereafter, said minimum shall not apply."

These are references, in my opinion, to this difference in the five and ten-year period, and also to the manner in which the contract may be terminated.

Then we have the paragraph 6 on page 5 of the same agreement, which gives Fisher, in the words "unrestricted right to terminate this agreement," and I think it is agreed that the proper notice provisions were followed. That is stipulated between the parties?

Mr. Allison: Yes, sir.

The Court: And then on page 6, the sixth line from the top of page 6, it says that when this notice, the 60-day notice is given, that "without further act of either parties and both parties shall be released from all further obligations hereunder, except," and then it lists three specific exceptions, and these involve royalty payments to Vickery.

And I feel that it is not necessary if you cite specific payments that must be made to go on and cite specific payments that can't be made or shouldn't be made, since I think when you release someone from all obligations except for the three specific ones, I think you have covered the field.

And then, of course, I think where the right to exercise the termination prior to the end of the five years, as set forth in paragraph 7 of the same agreement, then of course again there were specific conditions, basically, that Vickery get everything back.

And "8" again refers to the termination of the agreement, and Vickery shall be entitled to retain all

sums of money that he has already been paid, and I would certainly think he would be entitled to all sums of money that may still yet be due and owed to him. I don't think there is any controversy about that.

Now, again there is a way of terminating the contract if Vickery should die, which suggests again it could be done without the full ten-year wait.

Now, with respect to the Sales Agreement, Exhibit B, I think the crucial paragraph there has to do with the small paragraph on page 6, which is 13 lines from the bottom of page 6 of Exhibit B, and says, "In the event of cancellation of the aforesaid Royalty Agreement between the parties, this Agreement will be cancelled automatically," which would seem to affect Exhibit B if the proper cancellation provisions are carried out in Exhibit A.

Now, the only modification in "B" I find at all, and I think if the paragraph I have just read was not in here, might suggest why the parties re-offered a sales agreement to Vickery, after cancelling both agreements, which is the next paragraph which immediately follows the one above, "This Agreement," meaning Exhibit B, being cancelled automatically, in which it sets forth the sales agreement, and I read this to mean the sales agreement itself can't be cancelled without respect to the consideration of how the royalty agreement is to be cancelled, unless there is a showing made that Fisher didn't cancel it arbitrarily, "but in the exercise of reasonable discretion and in pursuance of the good faith hereinabove mentioned."

So on the matter of whether there is ambiguity or not, I don't feel there is any ambiguity, and there-

fore I think the termination given by the notice, and so forth, given by the defendant to the plaintiff, did terminate the contracts.

Now, the next consideration is whether or not there is some sort of fiduciary relationship that applies, whether there is some context outside of the actual wording of the contract itself that should be considered, and I think that the problem we have there, I think there is a developing field of law, which I have referred to earlier, which I see is in Corbin, in Section 1266, Corbin on Contracts, which I had read rather carefully in another case; as a matter of fact, in that case I ruled differently than I will be ruling here, because we dealt there with a franchise, and with an automobile manufacturer, or some manufacturer, and this is a very different situation; so I think in this case here we have two parties dealing with each other, through their lawyers, and unless the court, some other court besides this court, will read into the "unrestricted right to terminate," which are the words set forth in Exhibit A, will read into those words that there must be good faith, and that a termination must be reasonable under the circumstances, or that there must be a reasonable exercise of the discretion to terminate, unless the court will go that far, some other court besides myself, and read "the unrestricted right to terminate" is modified by that, as some courts have done in some of these franchise cases, and Congress has apparently done in this automobile dealers so-called "day-in-court" act; if that should be the case, then of course the whole matter is open on every other issue in this case.

I think what is open, then, is the question of whether the defendant in giving the termination acted in good faith, acted reasonably in doing it, and that would then go into the issue of fraud, or go into the issue of what the patents covered. It might even go into the issue of whether or not the plaintiff was performing the way he should perform under the contract; in other words, acting diligently in trying to help in the development in this whole area of valve inventions and improvements, and so forth and so on; so I think that this is the doorway, if there is to be a doorway, to go beyond the ruling that I may give here.

And I will say that I am not making this ruling simply to shorten the time, or not give you your day in court, or anything of that sort, because I don't believe it should be done that way, but if there is to be any benefit at all from the ruling I am about to make, at least it is a real simple short legal issue, which, if it is decided adversely to the way I rule here today, then you can launch on to the long trial which I think would have to follow, which would entail considerable expense, apparently 20 or 40 witnesses, many days in court, which would then not be too easy a situation on the party that doesn't prevail. Whereas in this particular instance, and I am not ruling this way for that reason, at least if there is any satisfaction to be gained, it is that I think that this is the doorway to a trial determination which will then stand on all of the other issues.

But I frankly don't believe that the contract is ambiguous; I think proper notice was given; I think

the unrestricted right to terminate does not contain within it an implied condition of any kind, or an act in good faith, or acting reasonably under the circumstances; or a reasonable exercise of discretion; and so, therefore, I would grant the defendant's motion for summary judgment with respect to whether or not they properly terminated the contract.

I don't know if there is anything else I need to say. The record sets forth fully what I believe here.

Mr. Kearney: Thank you very much, Your Honor.

The Court: Now, is there an accounting problem still as to what is owed under the terms of the contract as it now exists.

Mr. Kearney: Your Honor, we will stipulate to take care of that.

The Court: All right.

Mr. Allison: Well, we will stipulate to the amount. That is something else again. We claim that there is some \$15,000 in commissions due and owing under the contract, before the termination.

The Court: Well, what you could do is this: You could either stipulate to try to see if you can arrive at an agreement on that, or you could hold it off for further disposition as to any fact issues and law issues you might have on that.

Mr. Kearney: Well, I don't anticipate any difficulty in that, Your Honor. I stipulate that we will have our accountant submit their bill, and we will lean over backwards to compromise the situation.

The Court: Well, all I want to be sure is that you, on any remaining matters to be settled between

you—Certainly a motion for summary judgment can be granted, but it only goes to the issue of termination of this agreement. It doesn't settle any moneys that might be owing between you.

Mr. Allison: I understand that.

The Court: That is pretty obvious. So that if you can't settle that, I will be here, and if you feel that you must have a trial on that, or if you feel that you want to put it off, if you intend to appeal this whole matter, until the Circuit Court can decide whether what I decided here today was right or wrong, then you could, for example, if they should decide that I was wrong, you will have to go into the whole trial anyway.

Mr. Allison: Would you repeat that, Your Honor.

The Court: If they should decide that my ruling here today is wrong, then you would have to go into the whole trial in any case.

Mr. Allison: That is correct.

The Court: And it may be that you could hold in abeyance and both stipulate that if you can't agree and make any settlement without your waiving any rights to appeal this, then in that event you would hold it off until the 9th Circuit rules on this.

Mr. Kearney: I will so stipulate, Your Honor.

Mr. Allison: Now, Your Honor is going to be here?

The Court: I will be here until the middle of August.

Mr. Allison: So if we are unable to get together on the amount owed——

The Court: Yes, certainly, and that is why I am leaving it open to you, as to what you want to do.

Mr. Allison: Very well.

The Court: It seems to me it would make sense if you both can agree that if you can't settle without your client waiving any rights on what is owed under the contract so far, then the next thing to do would be to stipulate whether or not you can both agree to hold it off until you have an entire trial on this matter, in the event I am reversed; and in the event I am sustained, then just have a separate trial on just that issue.

Do you follow me?

Mr. Allison: Yes, sir.

The Court: I think that seems sensible.

Mr. Allison: Yes. Did I understand your Honor's ruling to preclude us introducing any evidence with respect to the fiduciary relationship between the parties, which is of course an independent tort apart from the breach of the contract on which Your Honor has ruled?

The Court: Well, I don't see how—Your plaintiff is an independent contractor who has dealt at arm's length, in entering into this agreement, and I don't think here is any dispute about this, by negotiations with the defendant, with both parties having a lawyer represent them; I don't think there is any dispute about that.

Mr. Allison: No question.

The Court: And I don't see, if they had a right to terminate under the terms of the agreement which each of them entered into, how there is by that reason any breach of any fiduciary relationship.

Mr. Allison: So your ruling goes to that?

The Court: Yes.

Mr. Allison: All right.

The Court: And I would include that in the ruling, that there has been no breach of any fiduciary relationship, because the defendant had a right under the existing contracts to terminate, and did terminate them lawfully and rightfully under the language of Exhibits A and B.

Mr. Allison: All right.

The Court: Now, of course, again if as part of these contracts is the matter of good cause, and there are conditions attached to it, which I don't see, then of course I think this is implicit in that, that that raises the question of whether there was a breach.

I don't know, it may be that the degree of care, the degree of good faith, the amount of what is reasonable under the circumstances, that might affect that standard, then, if that were introduced into it.

But I don't think, if they have a right to terminate it, I don't see any breach of anything, including any fiduciary relationship.

Mr. Allison: Thank you, sir.

The Court: Do you understand it?

Mr. Allison: Yes, I understand it.

The Court: Now, will you submit a form of judgment on this?

Mr. Kearney: Yes, sir, I will.

The Court: And I will be here in Courtroom 4.

Mr. Kearney: Thank you.

(The above-entitled matter was then recessed.)

No. 22,593

JULY 1 1968

In the

United States Court of Appeals

*For the Ninth Circuit*

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EDGAR HERBERT VICKERY,

*Appellant,*

vs.

FISHER GOVERNOR COMPANY,

*Appellee.*

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Reply Brief for Appellant

On Appeal from the United States District Court  
for the Northern District of California

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FILED

JUL 1 1968

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WM. B. LUCK, CLERK

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No. 22593

In the

# United States Court of Appeals *For the Ninth Circuit*

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EDGAR HERBERT VICKERY,

vs.

FISHER GOVERNOR COMPANY,

*Appellant,*

*Appellee.*

---

## Reply Brief for Appellant

On Appeal from the United States District Court  
for the Northern District of California

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Appellant ("Vickery") will reply briefly to some of the arguments made by Appellee ("Fisher") in its brief.

### I

#### **THE DISTRICT COURT ERRED IN THE STANDARD OF INTERPRETATION WHICH IT APPLIED TO THE AGREEMENTS**

In Paragraph 1 of Part III of Fisher's brief (pages 8-10), Fisher stoutly labors the obvious and never contested points that the Royalty and Sales Agreements contain termination

clauses and that Fisher insisted on the inclusion of such clauses in the agreements. Fisher also points out (page 9) that the District Court noted that Vickery had submitted to Fisher a proposed contract which excluded the right to terminate during the second five years of the term, that Fisher refused to accept this draft and, from this, the District Court concluded that Vickery signed the Royalty and Sales Agreements "Knowing that he (plaintiff) was giving defendant an unrestricted right to terminate." All of the foregoing begs the question at issue, which is: What did Vickery and Fisher *intend* by the use of the phrase in Paragraph 6 of the Royalty Agreement "Fisher has the unrestricted right to terminate this agreement at any time . . ."? (Appendix A, p. 5, Vickery brief). This is a question for judicial interpretation. As is emphasized in Vickery's brief at pages 5-7 and 32-33, the principal officers of Fisher represented to Vickery during the contract negotiations that this right of termination would be exercised only if Fisher determined that it could not manufacture and sell ball valves at a profit and that Vickery relied on those representations when he signed the agreements. In short, what Vickery intended by the above quoted phrase was what he thought Fisher intended, based upon the representations of its officers. That is, that Fisher had the unrestricted right to determine whether or not it could manufacture and sell ball valves at a profit. (In this regard, see Iowa Code, Section 622.22, which provides: "When the terms of an agreement have been intended in a different sense by the parties to it, that sense is to prevail against either party in which he had reason to suppose the other understood it.") The District Court sought to ascertain the intention of the parties from a mere reading of the Royalty Agreement, and concluded that the above quoted phrase

was susceptible of but a single meaning. Thus, the Court erred in applying the wrong standard of interpretation. Professor Wigmore points out (*Wigmore on Evidence*, Third Ed.) in Section 2458 that "The process of Interpretation is a part of the procedure of realizing a person's act in the external world." In Section 2460, he states that the standards of interpretation fall into four classes: (1) the popular standard, meaning the common and normal sense of words; (2) the local standard, including the special usages of a religious sect, a body of traders, etc.; (3) *the mutual standard, covering those senses which are peculiar to both of the parties to a transaction, but shared in common by them*; and (4) the individual standard of one party to an act, as different from that of the other party. He then analyzes these standards and concludes in Section 2462, page 194:

"There is, then, neither in theory, nor in policy any basis for an absolute rule declaring that when a word has a 'plain meaning', i.e., by the popular standard, neither the local nor the mutual nor the individual standard can be substituted. Such a rule is still maintained by many utterances like those above quoted. But its vogue is disappearing; as may be seen from the utterances of judges who have plainly championed the modern and more liberal rule."

In short, the District Court erred by applying the popular standard without consideration of the applicability of the mutual standard. Or, as stated in *3 Corbin on Contracts*, Section 535 (Quoted with approval in *Hamilton v. Wosepka*, *Ia.* ..., 154 NW 2d 164 at 168):

"It is true that when a judge reads the words of a contract he may jump to the instant and confident opinion that they have but one reasonable meaning and that he knows what it is. A greater familiarity with dictionaries and usages of words, a better under-

standing of the uncertainties of language, and a comparative study of more cases in the field of interpretation, will make one beware of holding such an opinion so recklessly arrived at."

## II

**THE DISTRICT COURT ERRED IN APPLYING THE PAROL EVIDENCE RULE TO PRECLUDE THE RECEPTION OF EVIDENCE NECESSARY FOR A PROPER INTERPRETATION OF THE AGREEMENTS**

As Fisher indicates on page 10 of its brief and as is evident from a reading of the transcript, the District Court concluded that parol evidence could not be introduced to vary what the Court previously had determined was the plain and unambiguous meaning of the phrase in question. This antiquated theory is thoroughly criticized by Professor Wigmore at Section 2461 and 2462. In *Hamilton v. Wosepka, supra*, a 1967 Iowa Supreme Court case which is more recent than all of the cases cited on this point by Fisher and which considers, in depth, the admissibility of parol evidence as an aid to the interpretation of a written instrument, the Court flatly held that extrinsic evidence that throws light on the situation of the parties, the antecedent negotiations, the attendant circumstances and the objects they were thereby striving to attain is necessarily to be regarded as relevant to ascertaining the actual significance and proper legal meaning of the agreement. In so holding, the Court quoted with approval from 3 *Corbin on Contracts*, Section 579 (at page 169 of 154 NW 2d) as follows:

"It is true that the language of some agreements has been believed to be so plain and clear that the court needs no assistance in interpreting. Even in these cases, however, it will be found that the court has had the aid of parol evidence of the surrounding circumstances. *The meaning to be discovered and*

*applied is that which each party had reason to know would be given to the words by the other party.* Antecedent and surrounding factors that throw light upon this question may be proved by any kind of relevant evidence. \* \* \* Such testimony does not vary or contradict the written words; it determines that which cannot be varied or contradicted. \* \* \*,” (Emphasis added)

In *Keding v. Barton*, ..... Ia. ...., 154 NW 2d 172, decided the same day as *Hamilton*, the court stated:

“Evidence of the circumstances [surrounding the making of the contract] is always admissible in aid of the interpretation of an integrated agreement. This is so even when the contract on its face is free from ambiguity.”

See also the concurring opinion of Justice Traynor in *Universal Sales Corp. vs. California Press Mfg. Co.*, 128 P2d 665, 20 C.2d 751, page 776, where he stated:

“I do not agree with the premise implicit in the majority opinion that parol evidence as to the meaning of the contract was admissible only because the contract is ambiguous on its face. Words are used in an endless variety of contexts. Their meaning is not subsequently attached to them by the reader but is formulated by the writer and can only be found by interpretation in the light of all the circumstances that reveal the sense in which the writer used the words. The exclusion of parol evidence regarding such circumstances merely because the words do not appear ambiguous to the reader can easily lead to the attribution to a written instrument of a meaning that was never intended. (Cal. Code Civ. Proc. Sections 1856, 1860; see Wigmore on Evidence 3rd ed., Sections 2458-2478; ‘The Theory of Legal Interpretation,’ 12 Harv. L. Rev. 417, by Oliver Wendell Holmes (then Chief Justice of Massachusetts.)”

## III

**FISHER'S INTERPRETATION OF THE AGREEMENTS PRODUCES ARBITRARY, UNFAIR AND ABSURD RESULTS WHICH COULD NOT HAVE BEEN THE INTENT OF THE PARTIES**

In Paragraph 3 of Part III of Fisher's brief (pages 12-16), Fisher attempts to support its argument that the exercise of its right of termination imposed substantial economic-business considerations by referring to provisions of the Royalty Agreement which are not relevant to the issue before this Court. There is no question that if Fisher had exercised the right of termination prior to October 1, 1965, Fisher would have had to give up valuable economic benefits pursuant to the provisions of Paragraph 7 of the Royalty Agreement set forth on Page 13 of Fisher's brief. But Fisher did not exercise its rights of termination prior to October 1, 1965; it was exercised on October 2, 1965. Accordingly, we are not concerned with the terms of Paragraph 7.

At page 14 of its brief, Fisher argues that the exercise of the right of termination after October 1, 1965 would mean a loss to Fisher of Vickery's consulting services to be rendered pursuant to Paragraph 5 of the Royalty Agreement and ". . . Fisher therefore had to elect whether Vickery's continuing technical contributions, if any, economically justified the amount of royalties which would have to be paid in consideration for his future services." This argument is fallacious. Paragraph 3 of the Royalty Agreement provides that royalties are to be paid only on net annual sales of products in excess of \$500,000. Thus, royalties are a function of sales, not services. In essence, Fisher is arguing for an interpretation of the Royalty Agreement which contemplates that the parties intended that Fisher should have the right during the first five years

of the term to develop products using Vickery's patent applications, patents, technical knowledge and know-how (with projected sales during the second five years of the term of \$64,210,000, see page 10, Vickery's brief) and also have the right, just when those developed products would have begun to bear fruit for Vickery in terms of royalties and sales commissions, to terminate the Royalty and Sales Agreements, thus suffering the "loss" of the technical knowledge of Vickery which Fisher already had obtained during the first five years of the term. In short, as Vickery pointed out in his opening brief, Fisher is contending for an interpretation which gives Fisher the unilateral option, during the second five years of the term, to pay or not to pay the royalty and sales commission consideration specified in the agreements.

At page 6 of its brief, Fisher also argues that the option to terminate after October 1, 1965 was "intended to provide Fisher with an important business alternative, namely, whether the benefits of Vickery's non-competition restriction . . . would economically justify the amount of royalties which would have to be paid for such benefits during the second five year period." Thus, Fisher asks this Court to believe that Fisher, which had the government granted monopoly of six United States Letters Patent covering the products in question (R. 328, lines 17-22), which owned all of Vickery's engineering drawings, which had obtained all of Vickery's technical know-how, which was a "long established manufacturer and distributor of a wide variety of valves, actuators and other related devices" (Fisher's brief, page 3) and which was tooled for and in production of products with projected sales during the next five years of \$64,210,000, actually made an "important" business decision to forego the restraint against the competition of Vickery, an individual, when Fisher terminated the agree-

ments. Interestingly enough, this consideration was never mentioned by any of the officers of Fisher whose depositions were taken.

Both of the foregoing arguments produce arbitrary, unfair and absurd results which are contrary to all established canons of judicial interpretation.

#### IV **FISHER'S FIDUCIARY DUTY**

On page 17 of its brief, Fisher suggests that Vickery's position that a party can breach a contract or any kind of a fiduciary duty by exercising an unrestricted right expressly reserved to it under a contract is an "unsettling proposition which would completely confuse otherwise orderly contractual arrangements." This proposition is no more "unsettling" than the provisions of the Uniform Commercial Code, set forth at page 35 of Vickery's brief, which impose on every contract "an obligation of good faith in its performance" and which authorize the courts to "so limit the application of any unconscionable clause as to avoid any unconscionable result."

On page 17 of its brief, Fisher states, without reference to record source, that Fisher invested "over \$1,000,000 in plant and equipment to develop the ball valve program." Vickery so alleged in Paragraph V of his initial complaint (R. 4), but not in his amended complaint. Fisher denied this allegation in Paragraph V of its initial answer (R. 37).

#### V **FISHER WILL NOT BE PREJUDICED BY THE GRANTING OF LEAVE TO VICKERY TO FILE AN AMENDED COMPLAINT**

On page 22 of its brief, Fisher claims that the granting of Vickery's motion for leave to file an amended complaint will result in prejudice to Fisher because it will require the reopening of discovery for the taking of the deposition of

Mr. Elfers. Vickery has no intention of taking his deposition and hereby expressly waives the right to do so. Since Mr. Elfers is a former officer and director of Fisher, Fisher obviously does not have to take his deposition. The depositions of all other persons concerning the issue of reformation have been taken. Fisher also suggests that new motions, pre-trial statements and trial preparation also will be required. The motions Fisher has in mind are not known to Vickery, but a single cause of action for reformation could not invite a complex or extensive motion. An amendment to the pre-trial statement to treat the allegations in *one* new pleading paragraph in the amended complaint and a new answer to treat that single paragraph certainly cannot be considered to be unduly burdensome. Similarly, the trial preparation for this new cause of action will be solely restricted to the determination of the Iowa law on reformation; a task that is far from monumental.

With respect to the portion of the District Court's Order quoted on pages 24 and 25 of Fisher's brief, it is apparent that the basis for the District Court's conclusion there expressed is that "the contract clearly expresses the real intention of the parties." Thus, the Court erred for the reasons set forth in Parts I and II of this brief.

## VI **CONCLUSION**

For the reasons stated herein and in Vickery's opening brief, it is respectfully submitted that the Orders of the District Court appealed from should be reversed.

Dated: June 25, 1968

EHRLICH & ALLISON

By EDWARD K. ALLISON  
Attorneys for Appellant

**CERTIFICATE**

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

EDWARD K. ALLISON

*Attorney at Law*

**No. 22593**

In the

**United States Court of Appeals**  
*For the Ninth Circuit*

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EDGAR HERBERT VICKERY,

*Appellant,*

vs.

FISHER GOVERNOR COMPANY,

*Appellee.*

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**Brief for Appellant**

On Appeal From the United States District Court  
for the Northern District of California

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**FILED**

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In the

**United States Court of Appeals**  
***For the Ninth Circuit***

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EDGAR HERBERT VICKERY,

*Appellant,*

vs.

FISHER GOVERNOR COMPANY,

*Appellee.*

}

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**Brief for Appellant**

On Appeal From the United States District Court  
for the Northern District of California

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**Jurisdictional Statement**

This is an appeal (i) from an Order Granting Motion For Summary Judgment in favor of Appellee (hereafter called "Fisher") made by the United States District Court for the Northern District of California and the judgment entered thereon on August 14, 1967 (R. 390) and (ii) from an Order (R. 482) of the same Court entered on December 18, 1967, denying the motions of Appellant (hereafter called "Vickery") (a) to set aside the Order Granting Motion For Summary Judgment and the judgment entered thereon and to grant Vickery a new trial pursuant to Rule 59(a), Federal Rules of Civil Procedure (hereafter F.R.C.P.), (b)

to vacate the Order Granting Motion for Summary Judgment and the judgment entered thereon, pursuant to Rule 59(e) F.R.C.P., and (e) for leave, pursuant to Rule 15(a), F.R.C.P., to amend Vickery's First Amended Complaint for Damages to add a second cause of action thereto for reformation of the agreements referred to therein.

Jurisdiction of the District Court was based on diversity of citizenship and the amount in controversy. 28 U.S.C. 1332 (a). Vickery is a citizen of the State of California. Fisher is a corporation incorporated under the laws of the State of Iowa and has its principal place of business in the State of Iowa. The matter in controversy exceeds, exclusive of interest and costs, the sum of Ten Thousand Dollars. Those jurisdictional allegations are in Vickery's Complaint For Declaratory and Other Relief (R. 1) and First Amended Complaint For Damages (R. 153) and are admitted in Fisher's Answer to Complaint (R. 36) and Answer to First Amended Complaint and Counterclaim (R. 160).

The District Court's Order Granting Motion for Summary Judgment (R. 390) contains the express determination that there is no just reason for delay and the express direction that judgment be entered (R. 391), specified in Rule 54(b), F.R.C.P. Accordingly, this Court's jurisdiction is conferred by 28 U.S.C. 1291.

### **STATEMENT OF THE CASE**

By his First Amended Complaint For Damages (R. 153), Vickery sought damages from Fisher in the District Court in the amount of \$1,131,376 for the breach of two agreements and for the breach of the fiduciary and confidential obligations of Fisher to Vickery imposed by these agreements, plus punitive damages in the amount of \$200,000. Both agreements are attached to the original complaint (R. 7-

35) and are incorporated by reference in the amended complaint (R. 154). One of the agreements, referred to in the amended complaint and herein as the "Royalty Agreement", is set forth in full (less Schedule "A" thereto) in Appendix "A" to this brief; the other agreement, referred to in the amended complaint and herein as the "Sales Agreement", is set forth in full in Appendix "B" to this brief.

The breach alleged is Fisher's termination of the Royalty Agreement pursuant to Paragraph 6 thereof, which termination also terminated the Sales Agreement by virtue of the provision of Paragraph 7 thereof (R. 156), and Fisher's continued manufacture and sale of the products covered by those agreements without payment to Vickery of the royalties and commissions specified therein (R. 156-157).

Approximately one year after the original complaint was filed, Fisher filed a Notice of Motion and Motion for Summary Judgment (R. 170) made "... on the ground that as a matter of law Defendant had an unrestricted right to terminate the contract which Plaintiff alleges was breached by reason of Defendant's notice of termination and there is accordingly no genuine issue as to any material fact." (R. 170, lines 25-29) Vickery filed an extensive Memorandum of Points and Authorities In Opposition To Motion For Summary Judgment (R. 178-264), including various declarations and documentary evidence in support of the allegations in the amended complaint, to which reference will be made below. The motion was argued before Judge Albert C. Wollenberg and by Order, dated November 18, 1966, (R. 296) the motion was denied.

Thereafter, the case was ordered for trial on July 19, 1967 before Judge Carl A. Muecke (R. 505), specially assigned from the United States District Court for the District of Arizona. On the day set for the trial, Judge Muecke soli-

cited a renewal of Fisher's motion for summary judgment (T. 59, lines 23-25) and granted it on the ground that Fisher's termination of the agreements was not a breach thereof (T. 72, line 22—T. 23, line 4) or of any fiduciary obligation of Fisher to Vickery (T. 76, lines 16-20).

The admitted and disputed facts and circumstances surrounding the negotiations of the Royalty and Sales Agreements, the performance by the parties thereunder and the termination thereof are as follows:

During the period from 1955 through the fall of 1960, Vickery developed, had manufactured for him and sold a line of quality ball valves with superior performance characteristics, principally to firms in the missile and aerospace industry. The selling prices of these valves ranged from \$2,000 to \$32,700 each. Prior to his association with Fisher, Vickery's sales of these valves amounted to \$889,633.91. The designs of these valves are covered by the patent applications and engineering drawings described in the Royalty Agreement. Vickery estimated that he invested \$115,801.23 of his own funds in the foregoing program (Vickery declaration, R. 226, line 23—R. 227, line 7).

During the latter part of 1960, Vickery and Fisher commenced negotiations which culminated in the contemporaneous execution of the Royalty and Sales Agreements. At the outset of these negotiations, Vickery disclosed his patent applications and valve designs to Fisher on a confidential basis (R. 193, lines 4-9). In general, the Royalty Agreement (Appendix "A") covered the sale by Vickery to Fisher of Vickery's interest in five applications for United States Letters Patent, certain engineering drawings and miscellaneous personal property, all of which related to ball valves previously developed and sold by Vickery, for a cash payment of \$100,000 (paragraph 2.3) and a royalty on sales

over a period of ten years, subject to earlier termination by Fisher (paragraph 3). The Royalty Agreement also covered the initiation and maintenance by Fisher of an aggressive development, engineering, manufacturing and sales programs for the ball valves covered by the agreement (paragraph 4). In general, the Sales Agreement (Appendix "B") covered the grant by Fisher to Vickery of the exclusive right to sell and service products covered by the Royalty Agreement to government end-users in the United States of America for a term of ten years for the commissions specified therein. The Sales Agreement provides (paragraph 7) that the termination of the Royalty Agreement would automatically terminate the Sales Agreement.

The subject of Fisher's right to terminate the Royalty and Sales Agreements prior to the expiration of the ten year term was thoroughly covered during the negotiations. In the Declaration of Alice Vickery (R. 253-255) and in the Declaration of Edgar Herbert Vickery (R. 226, lines 19-22), filed in opposition to Fisher's initial Motion for Summary Judgment (as to which Fisher filed no counter-affidavits or declarations), they state that this point was discussed by them at Fisher's office in Marshalltown, Iowa, with Mr. William Fisher, the president of Fisher, Mr. Paul Elfers, Mr. Kenneth Wolfe and Mr. Ray Engel, Fisher's Vice-Presidents, Mr. Cecil Johnson, Fisher's director of engineering, and Mr. H. R. Ponder, Fisher's treasurer. During the course of the discussion, it was agreed that the term of the agreements was to be for ten years, subject to termination at any time by Fisher. If Fisher terminated the agreements during the first five years of the term, all of the patent applications, designs and property which Vickery was to sell to Fisher would be returned to Vickery and Fisher would discontinue the sale of ball valves. If Fisher termi-

nated during the second five years of the term, Fisher would retain all of the patent applications, designs and property. Messrs. Fisher, Wolfe and Elfers all stated, however, that the only reason Fisher would terminate the agreements would be if Fisher could not sell the ball valves at a profit. Mr. Fisher explained that he was sure that if Fisher carried on a development, production and sales program for five years, Fisher would not want to give up ownership of the patent applications and designs even if Fisher did not intend to continue to manufacture and sell the ball valves covered thereby. Vickery discussed this point again with Messrs. Fisher, Wolfe and Elfers the following day and each of them assured Vickery that Fisher always dealt in good faith and that Fisher would not terminate the agreements unless Fisher determined that it could not manufacture and sell ball valves at a profit.

In his deposition (page 48, line 14—page 50, line 2; page 50, line 22—page 51, line 13), Mr. Fisher admitted that such assurances were given, but he claims that he stated that Fisher also would have the right to terminate the agreements if Vickery failed to communicate ideas to Fisher on a continuing basis. In his deposition (page 15, line 10—page 16, line 5), Mr. Wolfe also admits that such assurances were given but he “can’t recall” if any other reasons were expressed to Vickery. Mr. Elfer’s deposition was not taken. Mr. Ponder testified in his deposition (page 5, line 19—page 7, line 15; page 20, line 2—page 24, line 4) that the only reason he heard expressed by any Fisher representative to Vickery as the basis for the exercise of Fisher’s right to terminate the agreements was the possibility that Fisher could not manufacture and sell the products covered thereby at a profit.

On the basis of the assurances of these men, who the Vickerys knew were the major shareholders of Fisher and its principal officers and directors, the Vickerys ultimately executed the Royalty and Sales Agreements (Declaration of Alice Vickery (R. 255, lines 6-9) and Declaration of Edgar Herbert Vickery (R. 226, lines 19-22)).

Fisher's opinion of the valve designs which it had purchased from Vickery is set forth in the President's message to Fisher's stockholders in its 1960 Annual Report (R. 193), as follows:

"Negotiations were completed in the Fall to purchase a Ball Valve company on the West Coast. Since no factory properties or facilities were involved, the move to our Midwest location was relatively simple. The Vickery Ball Valve designs are the finest we have seen. The expansion of the Vickery concepts of design for applications at missile bases is now under full swing.

We have recently accepted our first orders for these sophisticated designs which must be submitted to complicated and unique tests before they will be released. The knowledge gained from such tests, coupled with our widespread experience in automatic control valves should provide an enviable position for your company."

After the execution of the Royalty and Sales Agreements, Vickery moved from his home in Oakland, California, to Marshalltown, Iowa, the site of Fisher's plant. There he worked with Fisher's personnel on the implementation of the ball valve program almost exclusively for approximately three and one-half years during the developmental phases of the program. Thereafter, he returned to California to concentrate for the next approximate year and one-half more exclusively on the sale of the products which had been developed (Vickery's declaration R. 227, lines 8-15).

During the course of Vickery's performance under the agreements, he worked initially in the development of what ultimately became known as the "Fisher-Vickery Ball Valve" and, thereafter, in the development of what ultimately became known as the "Hi-Ball Valve" (Vickery's declaration R. 227, lines 15-23). Vickery also re-designed the sealing mechanism for a valve which Fisher had commenced developing prior to Vickery's association with Fisher and which ultimately became known as the "Vee-Ball Valve" (Vickery's declaration R. 228, line 16 — R. 229, line 5). Vickery also invented a type of valve known as a "Cam-Ball valve" (Vickery's declaration R. 229, lines 17-21).

During the first five years of the term of the Royalty Agreement, the five patent applications referred to therein matured into six United States Letters Patent which issued in Fisher's name as assignee (R. 328, lines 17-22).

In the Declaration of Marcus Lothrop, Esq., Vickery's patent attorney, filed in opposition to Fisher's initial motion for summary judgment, he states that it is his opinion that one of those patents covers the "Fisher-Vickery Ball Valve", the "Hi-Ball Valve" and the "Vee-Ball Valve", with the exception of a certain model thereof which has no tight sealing means (R. 262-263). Fisher did not file a counter-affidavit or declaration to this declaration.

In Paragraph V of his amended complaint (R. 155), Vickery alleges that during the period from January 1, 1961 through December 31, 1965 (the first five years of the ten year term of the Royalty and Sales Agreement expired on October 1, 1965), Fisher's sales of products covered by those agreements within Vickery's exclusive territory under the Sales Agreement alone amounted to \$3,666,483, on which Fisher paid Vickery commissions in the amount of \$523,083. In Paragraph V of Fisher's answer (R. 161), Fisher admits

that these sales amounted to \$3,465,505 and that Fisher paid Vickery commissions thereon of \$515,805. Fisher claims that it does not have records of profits on all of these sales, but, with respect to the sales on which it admits it has profit records, Fisher made a pre-tax profit of \$336,469.72 on the \$2,533,992 sale price thereof (R. 256-257).

In addition to the foregoing sales of between \$3,666,483 and \$3,465,505 made by Fisher during the first five years of the term of the agreements, Fisher also admits the following sales during the same period of products which Vickery claims are covered by the Royalty Agreement (R. 328, line 30 — R. 329, line 12) :

*1963*

"Vee-Ball"*	.....	\$ 377,063
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*1964*

V-24 (predecessor of "Hi-Ball")*	.....	6,525
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"Vee-Ball"*	.....	537,991
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*1965*

"Vee-Ball"*	.....	1,709,774
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V-24 and V-25 (V-25 is "Hi-Ball")*	.....	17,830
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Total .....	\$2,649,183
-------------	-------------

\*Includes valve bodies and actuators and valves with and without seals.

\*Includes valve bodies and actuators.

Mr. Glenn Brockett, Fisher's Vice-President of Sales, testified in his deposition (page 18, line 19—page 19, line 2; and page 24, lines 1-5) that Fisher expected to make a pre-tax profit of at least 20% on "Vee-Ball" and "Hi-Ball" sales. This would amount to approximately \$529,836.

In addition, projections of the sales of products which Vickery contends are covered by the Royalty and Sales Agreements from January 1, 1966 (the effective date of Fisher's notice of termination was December 2, 1965) through December 31, 1970 (the ten year term of the Royalty and Sales Agreements would have expired on October 1, 1970) which were made by Fisher personnel at

or about the date of the notice of termination, or communicated by Vickery to Fisher prior to that date, are as follows:

“Vee-Ball Valve” .....	\$49,200,000
“Hi-Ball Valve” .....	9,135,000
“Fisher-Vickery Ball Valve”.....	4,000,000
“Cam-Ball Valve” .....	1,875,000
	<hr/>
	\$64,210,000

The projection of the “Vee-Ball Valve” sales is Exhibit B-3 to Mr. Brockett's deposition and he testified with respect thereto at page 12, line 10 — page 23, line 2. The projection of the “Hi-Ball Valve” sales is Exhibit B-4 to Mr. Brockett's deposition and he testified with respect thereto at page 23, line 3—page 24, line 10. The projection of the “Fisher-Vickery” and “Cam-Ball” sales are in Vickery's declaration (R. 229, line 17—R. 230, line 3).

Fisher's notice of termination (R. 35) was given on October 2, 1965. Paragraph 7 of the Royalty Agreement (Appendix “A”) provides, in substance, that if Fisher exercises the right of termination prior to October 1, 1965 (one day prior to the date of the notice of termination), Fisher shall be obligated to transfer to Vickery all personal property and designs, patent applications and patents received from Vickery, and to cease the production and sale of products covered by the Royalty Agreement. Under Paragraph 3 of the Royalty Agreement, Fisher's obligation to pay minimum royalties to Vickery ceased on October 1, 1965. Accordingly, from October 1, 1965 to the end of the ten year term (October 1, 1970), Fisher would be obligated to pay royalties to Vickery under the Royalty Agreement (Paragraph 3 of Appendix “A”) only to the extent that the annual sales of the products covered thereby exceeded \$500,000. Under the Sales Agreement (Appendix “B”), Fisher had no obligation to pay commissions to Vickery

unless Vickery sold products covered thereby within his exclusive territory.

Vickery was not informed that Fisher intended to terminate the Royalty and Sales Agreements until he received the notice of termination, although he was at Fisher's plant in Marshalltown in September, 1965, after the decision to terminate had been made (Vickery's declaration R. 230, lines 10-14). Mr. Brockett, Fisher's Vice-President of Sales, testified in his deposition in this regard (page 38, line 19—page 39, line 6) as follows:

- "Q. You have testified that you saw Mr. Vickery in Marshalltown in September of 1965 or the Fall of 1965?
- A. Yes.
- Q. Before the contract was cancelled.
- A. Yes.
- Q. Did you tell him at that time that the contract was going to be cancelled?
- A. No, sir.
- Q. Why not?
- A. He didn't ask me.
- Q. Well, don't you think in all fairness this would be a subject that you should bring up?
- A. No, sir."

At no time from the date Vickery signed the Royalty and Sales Agreements until he received the termination letter did anyone associated with Fisher complain, state or otherwise remark that the services Vickery was performing under those agreements were, in any manner, unsatisfactory (Vickery declaration R. 230, lines 4-9). In their depositions, Mr. Fisher testified that he made no such complaints (page 94, line 21—page 95, line 4), Mr. Engle, Fisher's Vice-President of Engineering, didn't recall any complaints (page 27, lines 17-19; page 29, lines 5-10) and

Mr. Johnson, Fisher's Director of Engineering, had no complaints (page 8, line 21—page 9, line 4).

The reasons why Fisher purported to terminate the Royalty and Sales Agreements were given by Messrs. Fisher and Brockett in their depositions taken approximately four months after the date of the letter of termination. Mr. Fisher testified that the decision to terminate the agreements was made at approximately the date of letter (October 2, 1965). Mr. Brockett testified that the decision to terminate was made in late July, 1965. The reasons given are vague, evasive, conflicting and insubstantial. Their testimony in this regard is set forth in full in Appendix C and Appendix D, respectively.

Neither Mr. Engle, Fisher's Vice-President of Engineering, nor Mr. Johnson, Fisher's Director of Engineering, was consulted about the advisability of exercising the right to terminate the Royalty and Sales Agreements and they were not advised that it had been exercised until some months thereafter. (Engle deposition page 29, line 11—page 30, line 7 and Johnson deposition page 10, lines 6-16).

On October 19, 1965, twelve days after the letter of termination was sent, Mr. Brockett wrote the following letter to Vickery (R. 264) :

“Dear Herb:

When I arrived home from Los Angeles, I found on my desk a copy of the letter from our attorney canceling your contract. I find that this was done as a result of instructions from Bill Fisher and Millard Gelvin. I did know that such a cancellation was under consideration, but I did not know that it was quite so imminent.

The real purpose of this letter is to advise you that as far as we are concerned, the cancellation of the contract will only affect the royalties and not our sales agreements. We will continue to accept orders from you and pay you the same commissions as in the past. Conse-

quently, I see no real reason for any fundamental change in our relationship."

Vickery did not respond to this letter.

### **SPECIFICATION OF ERRORS RELIED ON**

1. The District Court erred in granting Fisher's renewed motion for summary judgment.
2. The District Court erred in denying Vickery's motions to set aside and to vacate the Order Granting Motion For Summary Judgment.
3. The District Court erred in denying Vickery's motion for leave to file an amended complaint to add a second cause of action thereto for reformation of the Royalty and Sales Agreements.

### **QUESTIONS PRESENTED**

1. Whether a renewed motion for summary judgment (previously denied by another judge), which determined as a matter of law that a right to terminate certain agreements imposing a fiduciary and confidential relationship on the parties was exercised without liability, was properly granted on the day of trial (and motions to vacate and set the same aside were properly denied), when there were genuine factual issues as to the bad faith and lack of justification on the part of, and resulting benefit to, the terminating party and as to the resulting detriment to the terminated party.

2. Whether, regardless of the existence of a fiduciary and confidential relationship between the parties, a renewed motion for summary judgment (previously denied by another judge), which determined as a matter of law that a right to terminate certain agreements was exercised without liability, was properly granted on the day of trial (and motions to vacate and set the same aside were properly

denied), when there were genuine factual issues as to the bad faith and lack of justification on the part of, and resulting benefit to, the terminating party and as to the resulting detriment to the terminated party.

3. Whether a renewed motion for summary judgment (previously denied by another judge), based on the construction of certain agreements with a ten year term so as to give one party the unilateral option during the last five years of the term to pay or not to pay the specified consideration, was properly granted on the day of trial (and motions to vacate and set the same aside were properly denied).

4. Whether the District Court abused its discretion by denying Vickery's motion for leave to file an amended complaint to add a second cause of action to his First Amended Complaint for Damages for reformation of the Royalty and Sales Agreements, where the proposed amendment pleads essentially the same facts pleaded in the original and first amended complaints, no new discovery will be required and Fisher will not be prejudiced thereby.

### **APPLICABLE SUBSTANTIVE LAW**

The parties agree that the law of the State of Iowa governs all substantive issues in this case (R. 335, lines 25-26).

### **ARGUMENT**

1. The Royalty and Sales Agreement and the acts of the parties in connection therewith resulted in the imposition by law of a fiduciary and confidential relationship on the parties. That relationship obligated each of the parties to act toward the other in the utmost good faith and fair dealing. Fisher's termination of the Royalty and Sales Agreements was in bad faith and without justification, it re-

sulted in an unjust enrichment of Fisher and a material detriment to Vickery and, therefore, was a breach of this law imposed obligation.

### 1.1 The Fiduciary and Confidential Relationship:

1.11 During the course of the negotiations which culminated in the Royalty and Sales Agreements, Vickery disclosed his patent applications and valve designs to Fisher on a confidential basis (R. 193, lines 4-9). It is apparent from Paragraphs 4 and 5 of the Royalty Agreement and from the Sales Agreement that the parties intended to, and did, work together in a cooperative endeavor to develop, engineer, manufacture and sell ball valves of, or based upon, Vickery's designs. It is further apparent that Fisher gained additional knowledge with respect to Vickery's designs during the five years that Vickery and Fisher worked together in that regard (R. 227, lines 8-27; R. 228, line 16—R. 229, lines 5; R. 229, lines 17-21). The implementation of the whole ball valve program contemplated by the Royalty Agreement, from the developmental phase to the marketing phase, was within the exclusive control of Fisher (Royalty Agreement, paragraphs 4 and 5). Under circumstances such as these, the law imposes a fiduciary and confidential relationship on the parties.

See *Saco-Lowell Shops v. Reynolds* (4th Cir.) 141 F.2d 587 where the court stated at page 597:

"The liability of defendant here is not to be determined as upon a charge of patent infringement nor even as in the case of an ordinary licensee under contract for the payment of royalties, for the reason that the J frames upon which royalties are claimed embody not only the fundamental ideas embodied in the Reynolds invention but also a specific application of those ideas evolved by Reynolds himself and communicated to defendant because of the confidential relationship

into which the parties had entered for the development of the invention. In other words, defendant is not an independent manufacturer, nor is it a mere licensee manufacturing a machine obtained from an independent source. It is a licensee who was working with Reynolds in the joint enterprise of developing his machine for the market, and who brought out a machine based upon ideas which he conceived and which he communicated in aid of the joint enterprise. There can be no question but that defendant is liable for royalties on the machines embodying Reynolds' idea so communicated, quite irrespective of patent coverage or terms of the license agreement.

That there was a confidential relationship existing between defendant and Reynolds when they agreed to work together for the development and marketing of his invention is so clear as not to admit of argument. Cf. *Baker Oil Tools v. Burch*, 10 Cir., 71 F. 2d 31, 37. As said in the case cited, quoting from the note of Judge Hare in *1 Leading Cases in Equity* 62, 'Wher-ever one person is placed in such relation to another, by the act or consent of that other . . . that he becomes interested for him, or interested with him in any subject of property or business, he is prohibited from acquiring rights in that subject antagonistic to the person with whose interests he has become associated.'"

And *Stevens v. Marco*, 147 Cal.App.2d 357 (305 P.2d 669) where the court stated at page 373 (of 147 Cal.App. 2d):

"... Where an inventor entrusts his secret idea or device to another under an arrangement whereby the other party agrees to develop, patent and commercially exploit the idea in return for royalties to be paid the inventor, there arises a confidential or fiduciary relationship between the parties. [citing cases] Indeed, it would be difficult to postulate a relationship more confidential than one in which a secret is imparted to a

person professing to have the ability and facilities to develop, patent, and exploit it upon his promise to give the inventor a return in the form of royalties. In the instant case, the salutary character of such a rule is manifest. Plaintiff transferred to Marco a new and valuable idea and Marco assumed full responsibility for securing a patent. Since the processing of a patent application is secret, plaintiff could learn only what Marco cared to divulge about the progress of the Marco applications, as well as other applications on improvements, and he had of necessity, because of Marco's superior position in this respect, to repose a special confidence in Marco's integrity. In addition, since Marco was in charge of the marketing of the device, plaintiff had also to rely on his business judgment with respect to production, and on his fidelity with respect to keeping and furnishing honest accountings of sales. Here, too, Marco occupied a superior position. There was present, therefore, all the classic elements of a confidential relation, and Marco owed to plaintiff the fiduciary obligations of utmost good faith and fair dealing of one occupying a status akin to that of a trustee. As stated in *Cox v. Schnerr, supra*, 172 Cal. 371, 378, 156 P. 509, 513, 'And this rule [of fiduciary obligation] does not apply merely to those who bear a formal relation of trust to those with whom they deal—not only to attorneys, physicians, trustees, clergymen, kinsmen, and others who by the very force of their occupations or relationship are presumed to be in the class of persons bound to act with the utmost good faith. *It applies in every case "where there has been a confidence reposed which invests the person trusted with an advantage in treating with the person so confiding."*' (Emphasis added by the Court).

The Court then went on to point out that there was ample evidence from which the jury might also have found, as a matter of fact, that the parties were allied in an enterprise

similar to that of joint venturers for material gain which also would give rise to a fiduciary relationship.

To the same effect is *Hyde Corporation v. Huffines*, 158 Tex. 566 (314 S.W.2d 763), certiorari denied 358 U.S. 898 (79 S.Ct. 223). In that case, the parties entered into a licensing agreement covering a device on which a patent application had been filed. The term of the agreement was for one year with automatic renewals from year to year thereafter for the pendency of the patent application and for the life of any patent or patents that issued therefrom, subject to certain conditions not relevant to the decision. The agreement also provided "Sixty (60) days' notice to terminate this contract shall be given by Licensee." The Court stated at page 768 (314 S.W.2d) :

"It conclusively appears that as a result of this agreement and the negotiations preceding its execution, Hyde Corporation gained full knowledge of the Huffines device not only from the application for patent but from scale models, blue prints, and actual construction of the device. On May 31, 1955, when the parties were in the second year of operations under the contract, Hyde Corporation repudiated the licensing agreement by giving the sixty-day notice provided for in the contract. However, according to the jury's findings, said defendant did not cease to manufacture the Huffines' device but on the contrary continued to produce the same substantially in accordance with the description of the mechanism contained in Huffines' patent application."

The Court went on to state at pages 769-770 (314 S.W.2d) :

"Petitioner's arguments as to the pleadings and evidence [with respect to the issue of breach of confidence] seem to run counter to the realities of the case as fixed by the written licensing agreement. It is true

that there is no explicit written covenant contained in the contract which precludes petitioner from making use of information granted as a result of contract negotiations and disclosures by Huffines *after* the cancellation of the licensing agreement. It is also true that respondent's pleadings do not use the words 'in confidence' by way of stating a conclusion. The picture presented by the pleadings and the evidence both undisputed and as interpreted by the jury is that of a licensee after contracting with an inventor (in good faith according to the jury's answer to Special Issue No. 2) for the use of an invention upon which an application for patent was pending, repudiating the licensing agreement and insisting upon utilizing the device despite the fact that he secured information which enabled him to manufacture the device through the licensing agreement and the negotiations relating thereto. To say that petitioner did not gain knowledge of the device in this manner is to deny the stated purpose of the licensing agreement. . . . We are not called upon to consider at what period in the course of negotiations petitioner's actions may have ceased to be ethically permissible. We here have business relations culminating in a licensing agreement. The case seems to come squarely within the rule of the American Law Institute's Restatement of the Law that:

‘One who discloses or uses another’s trade secrets, without a privilege to do so, is liable to the other if  
(a) he discovers the secret by improper means, or  
(b) his disclosure or use constitutes a breach of confidence reposed in him by the other in disclosing the secret to him. \* \* \*.’<sup>4</sup> Restatement of Torts Section 757.

The jury evidently believed that at the time the licensing agreement was entered into, Hyde Corporation was acting in good faith, but thereafter decided to use the respondent's device without accounting to him. If so, it might be absolved under clause (a) of the rule

but would be held liable under clause (b) thereof. In the present case, the parties occupied the position of licensor and licensee. They were in a sense co-adventurers. There existed between them a confidential relationship as a matter of law and there was no need to submit these incidents of legal status to a jury for its determination. In commenting upon clause (b) of the rule above stated, it is said in the Restatement that:

‘A breach of confidence under the rule stated in this Clause may also be a breach of contract which subjects the actor to liability under the rules stated in the Restatement of Contracts. But whether or not there is a breach of contract, the rule stated in this Section subjects the actor to liability if his disclosure or use of another’s trade secret is a breach of the confidence reposed in him by the other in disclosing the secret to him. The chief example of a confidential relationship under this rule is the relationship of principal and agent (see Restatement of Agency, Sections 395 and 396). Such is also the relationship between partners or other joint adventurers. But this confidence may exist also in other situations. For example, A has a trade secret which he wishes to sell with or without his business. B is a prospective purchaser. In the course of negotiations, A discloses the secret to B solely for the purpose of enabling him to appraise its value. Or, A requests a loan from B, a banker, for the purpose of aiding the manufacture of a product by A’s secret process. In order to assure B about the soundness of the loan, A discloses the secret to him in confidence. In both cases B is under a duty not to disclose the secret or use it adversely to A.’ \* \* \*’<sup>4</sup> Restatement of Torts, Section 757, Comment on Clause (b) p. 13.

While there may be some distinction in the theory of recovery under clauses (a) and (b), that is whether in tort or contract, *Aktiebolaget Befors v. United States*, 90 U.S. App. D.C. 92, 194 F. 2d 145, that point is not involved here. In the area of confidential relationships

between partners, employers and employees, licensors and licensees, and the like, the injured party is not required to rely upon an express agreement to hold the trade secret in confidence, *Schreyer v. Casco Products Corp.*, 2 Cir., 190 F. 2d 921, *Smith v. Dravo Corporation*, 7 Cir., 203 F. 2d 369, nor should he be deprived of all relief because the offending person may have originally entered into the particular relationship unaffected by a then existing ulterior or improper motive."

The comment of the Restatement upon clause (b) makes it clear that the breach of confidence therein referred to is actionable separate and apart from any breach of contract.

The fact that the relationship in *Hyde* was licensor and licensee whereas here, Vickery assigned his patent applications and designs to Fisher and retained a royalty interest, does not distinguish the cases. See *Milligan v. Lalance & Grosjean Mfg. Co.* (Cir. Ct. N.Y.) 21 F. 570 which was a suit on a contract for royalties due under an assigned patent. There, the Court stated:

"The relation of the parties in respect to the patent became similar to that of licensor and licensee. The defendant held the legal title to the patent, but held it to use and pay for the use."

The principles expressed in the foregoing cases are followed in:

*Baker Oil Tools v. Burch* (10th Cir.) 71 F.2d 31, 36  
*Sloan v. Mud Products, Inc.* (N.D. Okla.) 114 F.Supp.  
 916, 926  
*Reddi-Wip v. Knapp-Monarch Co.* (E.D. Mo.) 104  
 F.Supp. 204, 209

In *Lukens Steel Co. v. American Locomotive Co.* (N.D. N.Y.) 99 F. Supp. 442 the Court expressly rejected the argument that a confidential and fiduciary relationship

cannot arise out of a business relationship between corporations experienced in business affairs. There, Lukens' engineers worked with the engineers of American ("Alco") in a cooperative endeavor to develop a certain type of locomotive. The court described the consequences of that relationship at page 446 as follows:

"It certainly was not a vendor and purchaser arrangement to which the rule of *caveat emptor* applies. Neither was it the formal relationship which exists between fiduciary and beneficiary, guardian and ward, or principal and agent. It appears in some respects to have some of the elements of a joint venture, but it is sufficient to say that it was a business relationship involving mutual confidence and mutual effort in which each party hoped to profit. Alco's goal was a competitively profitable engine block design. Lukens' goal was the future sale of its products. Although this Court can find no enforceable contract whereby Alco agreed to make any definite purchases for any definite time, or under any particular condition, it is readily inferable that Alco expected and intended to purchase at least part of its requirements from Lukens.

The problem next confronting the Court is the determination and application of the law which governs the conduct of the parties in the relationship found above.

Each case depends upon its own facts but speaking generally it may be said that when one reposes confidence in the skill or integrity of another who purports to act for the first party's benefit, then the actor may take no advantage to himself in hostility to the interest of the first party. A confidence reposed and accepted requires an undivided loyalty.

[The Court here quoted the excerpt from *1 Leading Cases in Equity* 62 quoted in *Saco-Lowell*, supra, as well as other authorities.]

Plaintiff's argument that the rule does not apply to the business relationship of these two large corpora-

tions experienced in business affairs is rejected. The fundamental concepts of honesty and fair dealing bind all business relationships in the various degrees required by the position of the parties and the extent of the confidence reposed. Theirs was not the 'arms length' dealing referred to in *Meinhard v. Salmon*, 249 N.Y. 458, 164 N.E. 545, 62 A.L.R. 1. The finding that confidence was reposed in Lukens and that both parties were interested in perfecting a suitable engine design makes the rule directly applicable."

Counsel could find no Iowa cases on this point which are factually similar to the case at bar; however, it is clear that Iowa recognizes fiduciary relationships arising from business transactions. See *Winn v. Rudy Patrick Seed Co.* 249 Iowa 431 (86 N.W.2d 678, 680) and *Goss v. Lanin* 170 Iowa 57 (152 N.W. 43, 45-46).

#### 1.2 The Extent of the Obligations Imposed by the Fiduciary and Confidential Relationship:

1.21 The consequences of the fiduciary and confidential relationship between Vickery and Fisher — which are imposed by law independently of the contractual rights and obligations of the parties — are succinctly stated in *Stevens v. Marco, supra*, at page 373 (147 Cal.App.2d):

"There were present, therefore, all of the classic elements of a confidential relation, and Marco owed to plaintiff the fiduciary obligations of utmost good faith and fair dealing of one occupying a status akin to that of a trustee."

1.22 Applying the foregoing principles to the instant case, it is clear that a confidential and fiduciary relationship existed between Vickery and Fisher. That relationship cast upon each party the law-imposed standard of "utmost good faith and fair dealing." Therefore, the facts and circumstances surrounding Fisher's termination of the Royalty

and Sales Agreements must be considered to determine whether Fisher's conduct met this standard.

1.3 The Following Circumstances Surrounding Fisher's Termination of the Royalty and Sales Agreements, as to Many of Which There are Genuine Factual Issues, Precludes the Granting of Summary Judgment:

1.31 The result of the termination was that Fisher appropriated to itself (i) six United States Letters Patent which were issued on the patent applications assigned by Vickery to Fisher pursuant to the Royalty Agreement (R. 328, lines 17-22), (ii) all of the ball valve and other designs disclosed in the engineering drawings described in Schedule "A" to the Royalty Agreement, (iii) the design of the "Cam-Ball Valve" invented by Vickery and disclosed to Fisher pursuant to the Royalty Agreement (R. 229, lines 17-21), (iv) the seal and other designs of Vickery embodied in the valves now manufactured and sold by Fisher under the trade names "Fisher-Vickery", "Hi-Ball" and "Vee-Ball" (R. 262-263), (v) the knowledge gained by Fisher from Vickery with respect to ball valve design and manufacturing techniques (R. 227, lines 8-27) and (vi) the market for ball valves in the missile and aerospace industry previously developed by Vickery (R. 226, line 23-R. 227, line 7), without paying to Vickery the royalties and commissions provided for over the remaining five years of the ten year term of those agreements.

1.32 Under Paragraph 3 of the Royalty Agreement, Fisher's obligation to pay minimum royalties to Vickery ceased on October 1, 1965 (one day prior to the letter of termination). Accordingly, if Fisher had not exercised the right of termination, Fisher would not have been obligated to pay any royalties whatsoever to Vickery unless Fisher's sales of products covered thereby exceeded \$500,000

annually. Similarly, under the Sales Agreement, Fisher had no obligation to pay commissions to Vickery unless he, in fact, made sales of the products covered by the agreements within his exclusive territory. Thus, the purported termination had no other effect than deprive Vickery of his royalties and commissions while permitting Fisher to unjustly enrich itself by enjoying all of the benefits of the agreements without the corresponding obligations.

1.33 During the first five years of the ten year term of the agreements, Fisher's sales of what Vickery contends are products covered thereby were between \$6,315,666 and \$6,114,688 (R. 161; R. 256-257; R. 328, line 30—R. 329, line 12), and Fisher's profit thereon exceeded \$866,305 (R. 256-257; Brockett deposition page 18, line 19—page 19, line 2; page 24, lines 1-5). Fisher terminated the agreements with the knowledge that the sales of what Vickery contends are products covered thereby over the remaining five years of the term of the agreements were projected to be \$64,210,000 (Brockett deposition page 12, line 10; page 23, line 2; page 23, line 3—page 24, line 10; Vickery declaration R. 229, line 17—R. 230, line 3).

1.34 Fisher's principal officers represented to Vickery during the contract negotiations that the right to terminate the agreements would be exercised only if Fisher could not manufacture and sell the products covered thereby at a profit (Declaration of Alice Vickery R. 253-255; declaration of Vickery R. 226, lines 19-22; Fisher deposition page 48, line 14—page 50, line 2; Page 50, line 22—Page 51, line 13; Wolfe deposition page 15, line 10—page 16, line 5; Ponder deposition page 5, line 19—Page 7, line 15; page 20, line 2—page 24, line 4).

1.35 Fisher regarded Vickery's ball valve designs as "the finest we have seen" and so stated in its 1960 annual report to its shareholders (R. 193).

1.36 Fisher did not inform Vickery that Fisher intended to terminate the agreements, although Vickery was in Fisher's offices after the decision to terminate had been made, at least according to the testimony of Mr. Brockett, Appendix D, (Vickery declaration R. 230, lines 10-14).

1.37 The reasons given by Mr. Fisher (Appendix C) and Mr. Brockett (Appendix D) for the decision to terminate the agreements are vague, evasive and contradictory. Among the reasons given were:

(a) Declining sales. In this regard, see Paragraph 1.33, *supra*.

(b) Lack or participation in and contribution to, the ball valve program by Vickery. But at no time prior to the termination did Fisher inform Vickery that any aspect of his ball valve designs or any respect of his performance under the agreements was unsatisfactory (Vickery declaration R. 230, lines 4-9; Fisher deposition page 94, line 24—Page 95, line 4; Engle deposition page 27, lines 17-19; page 29, lines 5-10; Johnson deposition page 8, line 21—page 9, line 4). Similarly, neither Mr. Engle nor Mr. Johnson, Fisher's Vice-President of Engineering and Director of Engineering respectively, who obviously would be most knowledgeable about Vickery's contributions to the program, were consulted about the advisability of exercising the right to terminate the agreements, nor were either of them advised that it had been exercised until some months after the event (Engle deposition page 29, line 11—page 30, line 7; Johnson deposition page 10, lines 6-16).

1.38 Fisher exercised the right of termination (R. 35) one day after October 1, 1965. If the right had been exercised by Fisher at any time prior to that date, Fisher would have been expressly obligated under Paragraph 7 of the Royalty Agreement to transfer to Vickery all personal property, designs, patent applications and patents received

from Vickery and to cease the production and sale of products covered by the Royalty Agreement.

1.39 Promptly after Fisher exercised the right of termination, Fisher offered to continue the Sales Agreement in effect (R. 264). Thus, it is apparent that the motivation for Fisher's exercise of the right of termination was to relieve itself of the obligation to pay royalties on the products developed from Vickery's designs on the enormous sales thereof which were projected for the remaining five years of the term of the Royalty Agreement. (Paragraph 1.33, supra)

1.4 The foregoing factual issues preclude the granting of a motion for summary judgment.

2. Fisher's termination of the Royalty and Sales Agreement was in bad faith and without justification, it resulted in an unjust enrichment of Fisher and a material detriment to Vickery and, therefore, was a breach of those agreements, regardless of the fiduciary and confidential relationship between the parties.

2.1 *Philadelphia Storage Battery Co. v. Mutual Tire Stores*, 161 So.Cir. 487 (159 S.E. 825) is the leading case for the proposition that the exercise in bad faith and without reasonable cause of an option to terminate an agreement with a fixed term is a breach of that agreement. In that case, the agreement was between a manufacturer and a jobber for a term of one year, terminable at any time by either party by written notice to the other. In the middle of the term and without prior notice, the manufacturer exercised the option. The manufacturer then sued the jobber for certain goods sold to the jobber. The jobber answered alleging that the manufacturer had cancelled the agreement pursuant to a fraudulent scheme to supplant him with another jobber, all in breach of the agreement. The manufacturer demurred to the answer on

the ground (as claimed by Fisher herein) that it had done nothing it was not authorized to do by the terms of the agreement. The demurrer was overruled and, on appeal from that ruling, the Supreme Court affirmed, stating in part:

“The clause relating to the right of cancellation of jobber’s agreement . . . is clear cut in its terms and free from ambiguity. It is enforceable if it be not against equity and good conscience. It would seem to be a necessary corollary that it may not be terminated, if the manner of its termination be against equity and good conscience.”

That case was followed in *Harrison & Sons, Inc. v. J. I. Case Co.* (E.D. So.Car.) 180 F.Supp. 243 and cited with approval in *Bernecker v. Bernecker*, Fla., 1952 (60 So. 2d 399).

*Audi Vision Inc. v. RCA Mfg. Co.* (2nd Cir.) 136 F.2d 621, involved the cancellation of an agreement which provided that it could be cancelled by one party “on written notice at any time”. The District Court granted a motion for summary judgment on this point in favor of the defendant and the plaintiff appealed. The Court of Appeals stated at page 622:

“On this appeal plaintiffs . . . contest the district court’s conclusion that defendant’s privilege of cancellation was unrestricted and that their allegations of defendant’s taking Audi Vision’s general manager into its employ, in order to get the benefits of the contract notwithstanding the cancellation, did not present any issue of fact.”

After concluding that it did not have jurisdiction to hear the appeal (for reasons which since have been corrected by amendments to Rule 54(b), F.R.C.P.) the Court stated at page 624:

“... In fact in the light of our necessary conclusion that the ruling heretofore made has been provisional only, the district court may well conclude hereafter upon further reflection that compliance with the cancellation provision may depend in part upon matters of fact as asserted by the parties, rather than exclusively upon the conclusion of law which it has heretofore made. Cf. 4 *Williston on Contracts*, Rev. Ed., Section 1027A; Restatement, Agency, Section 454; *White Co. v. W. P. Farley & Co.*, 219 Ky. 66, 292 S.W. 472, 52 A.L.R. 541; *Philadelphia Storage Battery Co. v Mutual Tire Stores*, 161 S.C. 487, 159 S.E. 825; 17 *Corn.L.Q.* 479; 45 *Harv.L.Rev.* 378.”

The concurring judge stated at page 626:

“As stated in the foregoing opinion, we have no jurisdiction to consider the merits of the appeal. Yet the opinion, although obliquely, in part suggests our views on the merits, for it broadly hints that the trial court should modify at least some of the rulings from which plaintiff sought to appeal. I may say that I, too, itch to discuss the merits and, if it were proper, would do so even more in detail. . . .”

*Philadelphia Storage Battery* is discussed with approval in 17 Cornell Law Quarterly 484, particularly at 479:

To the same effect as the foregoing cases is *Watkins v. Rich* 254 Mich. 82 (235 N.W. 845), where the Court stated at 846 (235 N.W.):

“A provision in a contract for termination at the option of one party is valid. But where the relationship is commercial and does not involve fancy, taste, sensibility, judgment, or other personal features, the option may be exercised only in good faith.”

See also Corbin on Contracts, Section 1266.

The case of *Shannon v. Gaar* 233 Iowa 38, (6 N.W. 2d 304), while involving an agreement at will rather than for a

fixed term, is analogous to the case at bar. There the principal terminated the services of a real estate broker shortly before the culmination of the negotiations and sale. The Court held that the broker had performed substantial services and could not be deprived of his commission by the mere termination of the agreement. Here, Vickery transferred all of his patent applications and designs to Fisher, communicated his know-how to Fisher and performed substantial services under the Royalty and Sales Agreements for a period of five years. Fisher's purported termination of the Royalty and Sales Agreements in the face of projections of enormous sales of the products covered thereby over the balance of the ten-year term of the Agreements, upon which Vickery would have earned substantial royalties and commissions, is comparable to the principal's termination of his broker's services in *Shannon* and the result reached in that case should be applicable here.

2.2 The facts and circumstances surrounding Fisher's termination of the Royalty and Sales Agreements (and Fisher's bad faith, lack of justification and unjust enrichment and Vickery's detriment in connection therewith, as to many of which there are genuine factual issues), are set forth in Paragraph 1.3, *supra*, and the existence of those factual issues precludes the granting of a motion for summary judgment.

3. The District Court's construction of the Royalty and Sales Agreements so as to give Fisher the unilateral option during the last five years of the term to pay or not to pay the specified consideration was erroneous as a matter of law.

3.1 Analysis and Construction of the Royalty and Sales Agreements.

3.11 Paragraphs 3 and 9 of the Royalty Agreement and Paragraph 7 of the Sales Agreement expressly provide for a term of ten years. Paragraph 7 of the Royalty Agreement

provides that if Fisher exercises the right of termination prior to October 1, 1965, Fisher *expressly* shall cease the production and sale of the products covered by the Royalty Agreement. The last paragraph of Paragraph 3 of the Royalty Agreement *expressly* provides that Fisher shall not be obligated to pay royalties to Vickery for products specified therein which are sold on orders accepted by Fisher on or after October 1, 1970. Paragraph 6 of the Royalty Agreement provides for Fisher's "unrestricted" right of termination; it also provides that if Fisher exercises the right of termination "both parties shall be released from all obligations hereunder" except for the obligation of Fisher to pay to Vickery (i) royalties on products which are shipped and billed prior to the date of termination, (ii) royalties on products sold from inventory on hand at the date of termination and shipped at any time thereafter and (iii) the pro-rata portion of the minimum royalty. While the Royalty Agreement *expressly* provides that Fisher shall cease production and sale if it terminates the agreement prior to October 1, 1965 and also *expressly* provides that Fisher can continue to manufacture and sell products after October 1, 1970 without royalty obligation to Vickery, nowhere in the agreement is the *express* provision that Fisher can terminate the agreement at any time after October 1, 1965 (which termination would also terminate the Sales Agreement pursuant to Paragraph 7 thereof) and continue to manufacture and sell products covered thereby without royalty or commission obligations to Vickery. If such an unfair result was intended (which is tantamount to a unilateral option for Fisher to pay or not to pay the specified purchase price for the property Fisher purchased) it certainly would have been set forth in express terms and not left to implication. The clause in Paragraph 6, paraphrased in (ii), above, militates against such a conclusion.

Could it have been intended that upon a termination of the Royalty Agreement by Fisher after October 1, 1965, that Fisher would have to inventory all of the products covered thereby then on hand, segregate the same from Fisher's continuing production, pay royalties to Vickery on the products so segregated (regardless of when they were sold) and not on the continuing production? This conclusion is compelled by the construction placed on the Royalty Agreement by the District Court and, yet, such a construction produces a result which is in conflict with commercial and practical reality and also has no apparent purpose.

The obvious purpose of the termination clause was to permit Fisher to terminate its express obligation to Vickery in Paragraph 4 of the Royalty Agreement to "maintain, during the effective period hereof, an aggressive development, engineering, manufacturing and sales program for ball valves" (and hence discontinue the production and sale of the products covered by the Royalty Agreement) should Fisher deem it unprofitable to continue to pursue that program and, since that decision is a matter of business judgment about which reasonable men can differ, Fisher was given the "unrestricted" right to make that decision. It is hornbook law that an agreement must be construed as a whole to give effect to all of the provisions therein. The foregoing construction is the only one possible which harmonizes the ten-year term of the Agreements and the clause relating to the payment of royalties on inventory on hand at the date of termination with the termination provisions. The foregoing construction also is in harmony with the representation made by Messrs. Fisher, Wolfe and Elfers to Mr. and Mrs. Vickery during the contract negotiations that the only reason Fisher would terminate the agreements would be if Fisher could not manufacture and sell the ball

valves at a profit (Declaration of Alice Vickery R. 253-255; Vickery declaration R. 226, lines 19-22).

On the other hand, the construction placed on the agreements by the District Court not only gives no effect whatsoever to the ten-year term of the Agreements which, obviously, is one of the most important provisions therein, but also results in giving Fisher, by construction of the Agreements, an unfair and unreasonable advantage over Vickery. This is contrary to the established canons of construction. See Williston on Contracts, Section 600, *Harvey Construction Co. v. Parmele* 253 Iowa 731 (113 N.W. 2d 760) and *Freese v. Town of Alburnett* 255 Iowa 1264 (125 N.W. 2d 790).

Also see the following cases which, by construction, limit the exercise of purportedly unrestricted termination clauses so as to achieve fair and reasonable results.

In *Richard Bruce & Co. v. J. Simpson & Co.*, 243 N.Y.S. 2d 503, an underwriter of securities which was obligated, "on a best efforts basis", to sell securities, had an agreement with the issuer which permitted the underwriter "in its absolute discretion" to terminate the agreement if the underwriter "shall determine that market conditions or prospects of the public offering are such as to make it undesirable or inadvisable to continue the public offer." The issuer refused to go forward with the offering and the underwriter sued for breach of the agreement. The issuer made a motion to dismiss on the ground that the agreement was illusory because of the underwriter's right to terminate. The Court denied the motion on the ground that the agreement was not illusory because "the term, 'absolute discretion', must be interpreted in context and means under these circumstances a discretion based upon fair dealing and good faith — a reasonable discretion."

In *Dubois v. Gentry* 182 Tenn. 103 (184 S.W. 2d 369) the Court said:

"Here it is expressly provided that the lessee shall have the right to terminate the lease 'for any reason' other than a wilful refusal to abide by it, or if the buildings are destroyed by fire. We cannot say that it could be terminated for a trivial reason, since in many circumstances such an excuse might amount to nothing more than a wilful act. If, however, the reason for its termination is founded in truth and fair dealing, then it is sufficient to justify the lessee in terminating his contract. Such a reason falls within the express provisions of the contract now before us. The words 'if for any reason', etc., as incorporated in the contract, should be construed to mean 'any good reason or just reason.'"

In *Quick v. Southern Churchman Co.* 171 Va. 403 (199 S.E. 489) the Court construed a provision in a contract which gave either party the right to terminate "for just cause" on 30 days' notice. The Court said "the grounds upon which [exercise of the right to terminate] is based must be reasonable, and there should not be an abuse of the conferred right. It must be a fair or honest cause or reason, regulated by good faith on the part of the party exercising the power. It limits the party to the exercise of good faith, based on just and fair grounds as distinguished from an arbitrary power."

The construction placed on the agreements by the District Court also is in diametric conflict with the covenant of good faith and fair dealing implied by law in every contract.

In 17A C.J.S. Contracts page 284-286 the rule is stated: "Moreover, in every contract there exists an implied covenant of good faith and fair dealing; and, more specifically, under such rule, the law will imply an agreement to refrain from doing anything which will destroy or injure the other party's right to receive the fruits of the contract."

In addition to the myriad of cases there cited in support of that statement, see also *Franke v. Wiltschek* (2nd Cir.) 209 F.2d 493 at 499, where the Court quotes with approval a statement by the authors of the Restatement of Torts, viz.: "But the tendency of the law, both legislative and common, has been in the direction of enforcing increasingly higher standards of fairness or commercial morality in trade. The tendency still persists."

In commercial transactions, Iowa clearly adheres to the policy expressed in the foregoing citation, as evidenced by its adoption (subsequent to the execution of the Royalty and Sales Agreements) of Sections 1-203 and 2-302 of the Uniform Commercial Code (respectively, 61 G.A.c. 413, Sec. 1203 and Sec. 2302) which provide:

"Section 1203. Every contract or duty within this code imposes an obligation of good faith in its performance or enforcement."

"Section 2302. (1) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination."

3.12 The construction placed on the agreements by the District Court—that during the last five years of the term Fisher had, in effect, the unilateral option to pay or not to pay the specified consideration—is so at odds with com-

mercial reality when compared with the construction herein placed on the agreements in Paragraph 3.11, supra, as to inexorably compel the conclusion that the agreements are ambiguous, that parol evidence must be received in aid of the interpretation thereof and that, therefore, summary judgment should not have been granted.

See *Aultman v. Meyers*, 239 Iowa 940 (33 N.W.2d 400) where the court stated at page 405 (33 N.W.2d) :

"The trust agreement was open to different constructions. On the face of the instrument there was some doubt, uncertainty and ambiguity. There was reasonable basis and fair debate as to its meaning on the part in question. It was susceptible to each of the constructions which the opposing parties placed on it. In such a situation it has uniformly been held by the court that not only evidence of the circumstances surrounding the parties and the transaction, and their conduct at the time, is admissible as bearing upon their intentions, but also what they may have said at or before the execution of the instrument which bears upon that intention. Such evidence does not change or contradict the wording of the instrument, but only explains, clarifies or removes any doubts as to its meaning. As said in *Chamberlain v. Brown*, 120 N.W. 334, 338: 'Of course oral testimony cannot be allowed to vary the terms of a written lease, but it is sometimes admissible in support of a contract to show in what manner it was understood by the parties who made it.' In *Seeger v. Manifold*, 231 N.W. 479, 481, the court said: 'It is also a well recognized rule of law that when the terms of a contract are ambiguous, then it is proper to look to the conversations, statements, circumstances, negotiations, and conduct of the parties as an auxiliary to the construction to be placed upon the same.' Like decisions will be found in many other cases, of which we cite the following. [citing 15 Iowa cases]"

4. The District Court abused its discretion by denying Vickery's motion for leave to file an amended complaint to add a second cause of action to his First Amended Complaint for Damages for reformation of the Royalty and Sales Agreements.

4.1 *The Nature of the Proposed Amendment:* The proposed second cause of action (R. 399-401) incorporates by reference all of the allegations in the first cause of action except those in Paragraph IV and adds one new Paragraph. The new paragraph (II) contains allegations concerning the representations made by the officers of Fisher to Mr. and Mrs. Vickery during the contract negotiations that Fisher would not exercise the right of termination unless, in Fisher's judgment, it could not manufacture and sell ball valves at a profit. Comparable allegations were made in Paragraph IV of the original complaint (R. 3) and in Paragraph IV of the First Amended Complaint for Damages (R. 155). The new paragraph then concludes with the allegation that, by the mutual mistake of the parties, the Royalty and Sales Agreements did not completely and accurately express that understanding (R. 400, line 29—R. 401, line 1).

4.2 *Procedural Authorities:*

4.21 The amendment of pleadings is governed procedurally by Rule 15(a), F.R.C.P. which provides in pertinent part:

“Otherwise a party may amend his pleading only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires.”

4.22 The quoted portion of Rule 15(a) is commented upon in Moore's Federal Practice, Second Edition (“Moore”) Section 15.08, at pages 874-875 as follows:

“Recognizing that the entire spirit of the rules is to the effect that controversies shall be decided on the

merits, the courts have not been hesitant to allow amendments for the purpose of presenting the real issues of the case, where the moving party has not been guilty of bad faith and is not acting for the purpose of delay, the opposing party will not be unduly prejudiced, and the trial of the issues will not be unduly delayed."

Here, Vickery cannot be charged with bad faith nor can he be charged with acting for the purpose of delay because it is to his obvious best interests to have this case decided as promptly as possible. Fisher would not have been prejudiced in any respect by the granting of the motion. The second cause of action in the proposed amended complaint pleads essentially the same facts as are pleaded in the amended complaint now on file. All discovery with respect to that complaint was completed and no new discovery will be required by either party. Accordingly, the trial of the issue would not have been delayed.

4.23 The proposed amendment cannot be objected to on the ground that the proposed second cause of action states a cause of action based upon the legal theory of reformation whereas the legal theory of the amended complaint now on file (which, as pointed out above, is identical to the First Cause of Action in the proposed amended complaint) is based on the legal theory of contract. This is made explicitly clear in Moore, Section 15.08, pages 876-880, as follows:

"Restrictions which state courts—or codes—have imposed upon the allowance of amendments have no place under the Federal Rules. Many jurisdictions, for instance, have followed the rule that an amendment may not 'substantially change' the cause of action or defense, or introduce a different claim or defense. This limitation has not been observed under Rule 15. \* \* \* Thus a complaint in an action under the Jones Act may be amended to bring the action also under the Death on

the High Seas Act; or a plaintiff, ordered to file an amended complaint, may include an additional cause of action arising out of the same transaction, *or may change the claim from one in contract to one for reformation in equity*, or to one in tort. The fact that an amendment involves a departure from the facts previously alleged is no bar to its allowance, since consistency in pleading is not required." (emphasis added)

**4.24** The fact that the proposed amendment is offered late in the case is not a ground for denying the motion to amend if the other party will not be prejudiced. See Moore, Section 15.08, pages 901-902 where it is stated:

"It should be particularly noted, however, that while laches and unexcused delay may bar a proposed amendment, the mere fact that the amendment is offered late in the case is not enough to bar it if the other party is not prejudiced. Amendments may be offered at the trial, or even after reversal and remand. In evaluating claims of prejudice, whether claimed by reason of delay or otherwise, the possible prejudice to the moving party if the motion is denied may also be weighed."

As is pointed out above, Fisher would not have been prejudiced by the granting of this motion and Vickery was severely prejudiced by the denial thereof by being denied the opportunity to have the issue of reformation decided on the merits.

#### *4.3 Substantive Authorities With Respect To Reformation:*

**4.31** The following authorities establish the law of Iowa with respect to the reformation of instruments:

*Wallace v. Spray* 248 Iowa 100 (78 N.W. 2d 406)

"The first prerequisite to plaintiff obtaining reformation of above instrument is the showing by clear and

satisfactory proof the existence of a contract between them, a meeting of the minds, as to what should be the terms of the subsequent written agreement. As will be later shown, there is a sharp conflict in the oral testimony of the two litigants. In such a situation the circumstances surrounding them and the relative reasonableness or unreasonableness of their respective versions properly may be considered and often furnish very satisfactory indication as to where the truth lies."

*Wormer v. Gilchrist* 210 Iowa 463 (230 N.W. 856)

"Equitable jurisdiction with reference to the reformation of a contract is well defined. If a written contract fails to express the true agreement of the parties thereto, then equity may be invoked, and if invoked will grant relief under proper circumstances without regard to the cause of the failure to express the contract as actually made, 'whether it be from fraud, mistake in the use of language, or any other thing which prevented the expression of the intentions of the parties.' (citing cases) It is said in *Costello v. Stokely Grain Co.* 186 N.W. 842, 843: To authorize a reformation there must be shown—'such a degree of proof as will produce, in an unprejudiced mind, the belief and conviction of the truth of the fact asserted, taking into consideration all the surrounding facts and circumstances.' (citing cases) In cases of this character the so-called parol evidence rule finds no application, and it is competent to show the conversations and the surroundings of the parties to the contract prior to its execution. A contract may be reformed to correct a clearly established mutual mistake, even though the party praying for reformation was guilty in a measure of negligence."

*Akkerman v. Gersema .... Iowa ....* (149 N.W. 2d 856)

"Of course, the right to reform an instrument is not absolute, but is within the sound direction of the equity

court and depends upon whether the remedy is essential to the ends of justice. *Milligan Co. v. Lott* [263 N.W. 262]. We said therein the facts and circumstances must be such as constitute an effectual appeal to the conscience of the court and prompt it to interfere by reformation to mitigate the rigorous rules of law."

*Walnut Street Baptist Church v. Oliphant* 257 Iowa 879 (135 N.W. 2d 97)

"If an instrument as written fails to express the true agreement between the parties, equity will grant relief, without regard to the cause of the failure to express the agreement as actually made, whether it is due to fraud, mistake in the use of language, or anything else which prevented the instrument from expressing the true intention of the parties."

*Miller v. Martin* 246 Iowa 910 (70 N.W. 2d 141)

"However, there is no question but that a court of equity may reform an instrument when it fails to express the true agreement of the parties. Relief may be granted without regard to the cause or reason for failure to express, in the written agreement, the agreement actually made whether due to fraud, mistake in the use of language, or any other thing that prevented the expression of the true agreement. *Coleman v. Coleman* 133 N.W. 755; *Milligan Co. v. Lott* 265 N.W. 262"

To the same effect is *Costello v. Stokely Grain Co.* 193 Iowa 203 (186 N.W. 842).

#### 4.4 *The Facts And Law Establish That Vickery Is Entitled To Reformation:*

Throughout this action—in the original complaint, in the first amended complaint, in the proposed amended complaint, in the depositions of Vickery and his wife and in the Declarations of Vickery and his wife filed in support of the

motion (R. 419; 421-425)—Vickery has consistently stated that during the negotiations which preceded the execution of the Royalty and Sales Agreements, the *only* reason assigned by any representative of Fisher for the inclusion of a termination clause in the Royalty Agreement was to enable Vickery to relieve itself of its continuing obligations in the event it could not manufacture and sell the products covered thereby at a profit.

If Vickery's version of the statements made to him during the negotiating meetings (i.e., that Fisher would terminate the Agreements *only* if the products covered thereby could not be manufactured and sold at a profit) are believed by a court or jury, it is clear that the parties' oral agreement to this term of the contract was restricted to termination for that reason and that reason alone, even assuming that Fisher had other reasons which it did not disclose. See Iowa Code, Section 622.22 which provides:

“When the terms of an agreement have been intended in a different sense by the parties to it, that sense is to prevail against either party in which he had reason to suppose the other understood it.”

In *Castner v. First National Bank of Anchorage* (9th Cir.) 278 F. 2d 376 at 384 the Court stated:

“In view of our conclusion that the record tends to show the existence of facts permitting appellant to maintain this action, the Court below should not have entered the summary judgment against the appellant. For where the entire record reveals facts susceptible of inferences that would justify an amendment of the pleadings and save the action, a motion for summary judgment should not be granted, but the party against whom the motion is directed should be afforded an opportunity to amend his faulty pleading. *Kane v.*

*Chrysler Corp.*, D.C. Del. 1948. 80 F. Supp. 360; *Ros-siter v. Vogel*, 2 Cir., 1943, 134 F. 2d 908, 912. Accordingly, the judgment will be reversed and appellant permitted to amend her complaint to show, if possible, the facts suggested in her affidavit."

Certainly, the foregoing "reveals facts susceptible of inferences that would justify an amendment of the pleadings" within the meaning of the above quotation from *Castner*.

### **CONCLUSION**

For the reasons stated above, it is respectfully submitted:

1. That this Court should reverse the Order Granting Motion For Summary Judgment made by the District Court and the judgment entered thereon on August 14, 1967 and, in so doing, determine, as a matter of law:

- a. That the Royalty and Sales Agreements imposed a fiduciary and confidential relationship on the parties which precluded the termination thereof by Fisher unless Fisher acted in the utmost good faith and with reasonable justification;
- b. That, in any event, Fisher did not have the right to terminate the Royalty and Sales Agreements unless Fisher acted in good faith and with reasonable justification;
- c. That the termination provisions of the Royalty and Sales Agreements are ambiguous and parol evidence should be received by the District Court in aid of the interpretation thereof.

2. That this Court should reverse the Order made by the District Court made on December 18, 1967 and direct that Vickery be granted leave to file an amended complaint

to add a second cause of action for reformation of the Royalty and Sales Agreements.

Dated: April 25, 1968.

EHRLICH & ALLISON

By EDWARD K. ALLISON

*Attorneys for Appellant*

**CERTIFICATE**

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

EDWARD K. ALLISON

*Attorney at Law*





## ***Appendix A***

### **AGREEMENT**

**AGREEMENT**, effective as of October 1, 1960, by and between **FISHER GOVERNOR COMPANY**, a corporation, the principal office of which is in Marshalltown, Iowa, (herein called "Fisher") and **EDGAR HERBERT VICKERY**, whose office address is 610 Sixteenth Street, Oakland, California (herein called "Vickery").

### **RECITALS**

A. Vickery has developed various types of ball valves and related actuators and devices (herein, for convenience, referred to collectively as "ball valves") some of the elements, features and characteristics of which are described in the following applications for United States Letters Patent made by Vickery:

<b>Serial Number</b>	<b>Filing Date</b>	<b>Short Description</b>
614,842.....	October 9, 1956	Ball valve
677,617.....	August 12, 1957	Liquid oxygen valve and actuator
749,770.....	July 21, 1958	Ball valve
812,309.....	May 11, 1959	Sealed ball valve
39,846.....	June 30, 1960	Protected ball valve seal,

and the balance of which are described in the engineering drawings described in Schedule A attached hereto. Vickery also is the owner of the following test units:

- Two 3" Aluminum ball valves (BBV-300)
- One 3" Stainless steel ball valve (BBV-300A)
- One 3" Stainless steel Ball valve with actuator (MB-31503-S115),

and miscellaneous jigs, fixtures, cutting tools and parts which are useful in the manufacture of ball valves.

B. Fisher desires (i) to purchase all of Vickery's right, title and interest in and to the patent applications, engi-

neering drawings, test units and miscellaneous equipment described in Paragraph A and (ii) to engage in the business of manufacturing, using and selling the ball valves covered thereby.

The parties, therefore, agree as follows:

1. Vickery—

1.1 hereby sells, assigns, transfers and sets over unto Fisher all of Vickery's right, title and interest in and to the patent applications, engineering drawings, test units and miscellaneous equipment described in Paragraph A; and

1.2 warrants that he owns and has the right to sell the same free and clear of any interest of any third party; and

1.3 agrees forthwith to deliver to Fisher copies of the originals of said patent applications (including all correspondence and documents related thereto) and said engineering drawings, tests units and miscellaneous equipment.

2. Fisher—

2.1 hereby purchases the patent applications, engineering drawings, test units and miscellaneous equipment described in paragraph A; and

2.2 agree to continue to prosecute, at its expense, each of said patent applications so long as the patent counsel for Fisher believes that the continued prosecution thereof will result in the issuance of a patent; and

2.3 agrees to pay Vickery therefor

2.31 \$25,000.00 in cash, promptly after receipt by Fisher of the property to be delivered to it pursuant to Paragraph 1.3 and \$75,000.00, in cash on January 15, 1961.

3. As soon as reasonably feasible, after the execution hereof and delivery of the foregoing items unto Fisher, it will proceed to the manufacture and sale of Vickery Ball Valves (or under whatever designa-

tion or name Fisher may see fit), and, during an initial period of ten (10) years beginning on October 1, 1960, subject to termination prior to the end of said period as hereinafter set forth, Fisher shall pay unto Vickery, his heirs, assigns or designees, royalties upon sales of said ball valves, as follows:

Two percent (2%) of all net annual sales in excess of \$500,000 and not in excess of \$1,500,000,

One and a half per cent (1½%) of all net annual sales in excess of \$1,500,000 and not in excess of \$2,500,000,

One percent (1%) of all net annual sales in excess of \$2,500,000.

with the further agreement that, during the first five years of said ten year period, or during such lesser period as this contract may be in force; Fisher shall pay no less than \$20,000.00 of royalties per year, in any event; and, thereafter, said minimum shall not apply.

"Net annual sales," for the purposes hereof, is defined to mean the aggregate of the sale prices of the products specified herein (less sales commissions paid on said sales, but inclusive of cash and prompt payment discounts allowed) billed by Fisher, its successors, subsidiaries and licensees, at any time for said products which are shipped (i) during the contract year ending on the anniversary of the effective date of this agreement and during each succeeding contract year to and including the contract year ending on October 1, 1970, and (ii) during each contract year after October 1, 1970 on orders which are accepted by Fisher prior to October 1, 1970.

Royalty payments shall be made within sixty (60) days after the end of each quarter calendar year. Since the exact amount due cannot be known except at the end of each full year of the period of this agreement, Fisher will not be held to pay more than \$5,000.00

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in royalties at the end of each quarter calendar year during the first five years of this contract with final adjustment to be made at the end of each year; or, during the remaining period of this contract, more than one-fourth of estimated annual royalties at the end of each quarter calendar year, Fisher to have the right to make such estimates and to provide a reasonable margin of safety for errors in estimates; again, with final adjustment to be made at the end of each year of this agreement.

At the end of each year of this contract, with each final royalty payment for the preceding year, Fisher shall furnish to Vickery, or his successors in interest, a brief statement showing the basis for the royalty payments for such preceding year. Vickery, or a representative chosen by him, shall have the right, at all reasonable times and, in such manner as not unduly to inconvenience Fisher, to inspect and check the sales records of Fisher in respect to the sale of ball valves for the purpose of verifying the amount of royalty payments, or ascertaining royalties due.

Fisher shall not be obligated to make any royalty payments to Vickery for products specified herein which are sold on orders accepted by Fisher on or after October 1, 1970.

4. Fisher agrees that after the delivery to it of the property herein specified it will promptly initiate and thereafter maintain, during the effective period hereof, an aggressive development, engineering, manufacturing and sales program for ball valves.

5. In order to acquaint Fisher personnel with the highly technical and intricate techniques involved in the design and manufacturing of ball valves and to assist in the implementation of the ball valve program, Vickery agrees that for the period during which royalties are payable hereunder he will, without further consideration:

Serve as a consultant to Fisher in the development, engineering, manufacturing and sale of ball

valves and to devote as much time thereto as Fisher may require.

Attempt diligently and continuously to develop improvements in respect of ball valves, disclose all of such improvements to Fisher promptly after Vickery conceives of the same, and, if directed by Fisher and at Fisher's expense, make application for letters patent on any or all of such improvements and assign the same to Fisher.

Refrain from any act or conduct whatsoever which, directly or indirectly, involves competition or interference with Fisher in the development, engineering, manufacturing or sale of ball valves. If Fisher does not exercise its right to terminate this agreement pursuant to the terms hereof, this obligation shall continue indefinitely.

6. Fisher has the unrestricted right to terminate this agreement at any time by giving Vickery at least sixty (60) days prior written notice by U.S. Registered Mail addressed to Vickery at his last known address. If Fisher exercises its right of termination within the period and in the manner specified, this agreement shall terminate sixty (60) days after the date on which such notice is mailed or on the date specified in the notice, whichever is later, without further act of either party and both parties shall be released from all further obligations hereunder, excepting as follows:

Fisher shall continue to be obligated to:

pay to Vickery within ninety (90) days after the date of termination all royalties which may be due on products specified in Paragraph 3 which are shipped and billed on or prior to the date of termination; and

pay to Vickery within ninety (90) days after the date of shipment all royalties which may be due on products specified in Paragraph 3 which are sold from inventory on hand at the date of termination

and shipped or accepted for shipment at any time thereafter; and

pay to Vickery within ninety (90) days after the date of termination the proportion of any installment of minimum royalties specified in Paragraph 3 which would be due at the end of the quarter annual year during which this agreement terminates which the number of days in that quarter annual year prior to the date of termination bears to the total number of days in that quarter annual year, but thereafter no further minimum royalties shall be payable by Fisher.

7. In the event Fisher exercises the right of termination prior to October 1, 1965, then and in such event Fisher shall be obligated to:

transfer to Vickery, promptly after the date of termination, all of Fisher's right, title and interest in and to all physical property delivered to Fisher pursuant to Paragraph 1.3 which then is in existence, together with all designs and data in its possession relating to ball valves, free and clear of any interest of any third party and to deliver the same to Vickery; and

assign and deliver to Vickery, promptly after the date of termination, all patent applications and patents which may have been issued thereon which  
(i) are assigned to Fisher pursuant hereto and  
(ii) may be assigned to Fisher pursuant to the terms hereof; and

forthwith permanently cease the production and sale of any of the products specified in the above Paragraphs, except such products as Fisher may have in inventory on hand at the date of termination.

8. In the event of the termination of this agreement Vickery shall be entitled to retain all sums of money theretofore paid to him under the terms hereof.

9. For the sole purpose of protecting the right of Vickery to receive the royalties provided for herein and without intending otherwise to restrict the absolute ownership by Fisher of the property transferred to it and which may be transferred to it pursuant hereto, Fisher agrees that it will not prior to October 1, 1970, without the prior written consent of Vickery, sell, transfer, license or otherwise dispose of any of its rights in any of said property; provided, that nothing herein shall prohibit such a sale, transfer, license or other disposition by Fisher to a wholly-owned subsidiary of Fisher, a successor of Fisher by merger or consolidation, or to an individual or entity which is a licensee of Fisher under a license agreement which is presently in effect; provided further, that the subsidiary or successor shall assume the obligations of Fisher under this agreement and, in the first such instance, Fisher shall guarantee the performance of said obligations by the subsidiary. In the event of an authorized sale, transfer, license or other disposition, the subsidiary or successor or other third party shall not have the right to make any further sale, transfer, license or disposition without the prior written consent of Vickery.

10. Vickery shall bear full risk and responsibility for defending any patent infringement suit or suits brought against Fisher and Vickery further agrees to indemnify and hold Fisher harmless against any damages, loss or expense sustained by Fisher as a result of any infringement suit whatever. Vickery's liability hereunder shall be limited to the amount of any royalties which may be due and owing him at the time of the institution of such suit or suits.

11. In the event Vickery should die during the term of this agreement, his death shall not terminate or otherwise affect Fisher's obligations hereunder and all sums of money which thereafter may become due

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to Vickery hereunder and all property which thereafter Fisher may be obligated to transfer and deliver to Vickery hereunder shall be paid, transferred and delivered to Vickery's heirs, or to the person or persons entitled thereto under any decree of distribution entered in the probate administration of Vickery's estate. Payment transfer and delivery made by Fisher to said heirs or person or persons shall completely absolve Fisher from any further obligation with respect thereto. If, after Vickery's death, Fisher elects to exercise the right to terminate this agreement, the notice of termination shall be effective if it is mailed by U. S. Registered Mail addressed to Vickery at his last known address or, if the executor, administrator or other personal representative of Vickery's estate or Vickery's heirs gives written notice to Fisher of another address to which such notice of termination should be sent, then to that address.

**12. In the event that Fisher—**

fails to perform any of its obligations hereunder and fails to remedy the same within sixty (60) days (fifteen (15) days in the case of a failure to pay any sum which is due to Vickery hereunder) after receipt by Fisher of written notice thereof from Vickery; or

voluntarily files a petition in bankruptcy or for reorganization or to effect a plan or other arrangement with creditors under any bankruptcy or similar law or makes an assignment for the benefit of its creditors; or if a petition in involuntary bankruptcy is filed against Fisher or if any other type of proceeding for the benefit of creditors is commenced against Fisher or if a receiver or trustee is appointed to take charge of all or a substantial portion of the assets of Fisher and if such last mentioned petition or proceeding is not dismissed or if such receiver or trustee is not discharged

within sixty (60) days after filing or appointment, respectively, then,

Vickery shall have the right to terminate this agreement by written notice to Fisher, but such termination shall not affect the obligations of Fisher. The exercise of the rights granted to Vickery in this Paragraph shall not preclude Vickery from asserting any other legal rights which Vickery may have under the circumstances.

13. With respect hereto Vickery shall be an independent contractor and it is expressly understood that Vickery is not an employee of Fisher.

14. The validity of this agreement shall be determined by and this agreement shall be construed in accordance with the laws of the State of Iowa.

15. This agreement (i) shall be binding upon and inure to the benefit of the successors and assigns of Fisher (subject to the provisions hereof) and (ii) shall be binding upon and inure to the benefit of the personal representative, heirs, successors and assigns of Vickery.

IN WITNESS WHEREOF, Fisher has caused this agreement to be subscribed by its duly authorized officers and Vickery has hereunto set his hand on the respective dates set opposite their names, but effective as of October 1, 1960.

FISHER GOVERNOR COMPANY

By /s/ J. W. FISHER  
*Its President*

Attest: /s/ G. BUTLER  
*Its Secretary*

November 10, 1960

/s/ EDGAR HERBERT VICKERY  
Edgar Herbert Vickery

November 5, 1960

**CONSENT, WAIVER AND AGREEMENT**

For the purpose of signifying her acquiescence to all of the foregoing, and waiving any rights which she has, or may have in the premises, arising out of the community property laws of the State of California, and as an inducement to Fisher, ALICE M. VICKERY, wife of Vickery, does hereby join in the execution of this agreement; and she agrees that Fisher may deal in this matter, in whatever respect, solely with Vickery and make all payments due hereunder to him alone, or to his designees or successors in interest, without reference to her.

Dated: November 5, 1960

/s/ ALICE M. VICKERY  
Alice M. Vickery

**Appendix B****AGREEMENT**

AGREEMENT, effective as of October 1, 1960, by and between FISHER GOVERNOR COMPANY, a corporation, the principal office of which is at Marshalltown, Iowa, (herein called "Fisher") and EDGAR HERBERT VICKERY, whose office address is 610 Sixteenth Street, Oakland, California, (herein called "Vickery").

The parties agree as follows:

1. Fisher hereby grants to Vickery the right to sell and service Fisher manufactured ball valves with the exclusive right to sell such ball valves to government end-users in the United States of America.

1.1 A "Ball Valve," for the purposes, hereof, is defined to mean any of the products specified in the separate Agreement, effective as of October 1, 1960, between the parties hereto, including replacement parts therefor.

1.2 A "government end-user," for the purposes hereof, is defined to mean—

1.21 Any agency or department of the government of the United States of America, or

1.22 Any contractor of any such agency or department, or

1.23 Any known subcontractor of any such contractor.

1.3 "Government use," for the purposes hereof, is defined to mean the application of ball valves in—

1.31 Aircraft, spacecraft and missile systems (including test, facility, transport, support and launching systems related thereto); or

1.32 naval vessel, submarine and other maritime systems; or

1.33 atomic energy research, test and experimental systems; or

1.34 military equipment systems.

2. Unless otherwise agreed in writing by the parties, Vickery's representation hereunder is limited to the sale of ball valves to government end-users for governmental use.

3. Fisher will pay commissions or extend a preferential discount to Vickery on prices f.o.b. Marshalltown, Iowa, as hereinafter provided:

- |  |     |
|--|-----|
| (a) On standard published price items sold at Consumer's Net .....   | 15% |
| (b) On standard items sold at 10% beyond Consumers Net .....   | 10% |
| (c) On items sold at 15% or 20% beyond Consumer's Net .....  | 5%  |
| (d) On special items not carried as standard priced items, it is the intent to build into the selling price a commission or earning power of 15% on the sales or contract price. If, because of competitive or contract requirements, it is not possible to include a 15% sales commission, such contracts, pricing or quotations for sale shall carry a lesser amount of commission. Such amount as may be available will be determined by Fisher which will advise Vickery during the course of arriving at the price of items to be quoted or sold. |     |
| (e) Replacement Parts — On standard equipment when sold at Consumer's Net.....   | 15% |
| (f) Replacement Parts — On standard equipment when sold at Consumer's Net less 10%..   | 10% |
| (g) Commissions will be shown on credit memorandums at the time of invoicing. Payment will be made on the 15th day of the second month following the month of invoicing. Commissions paid on any uncollectible account will be debited to Vickery and other representatives who may have participated in the original commission payment. Any billing to representatives will be payable on or before the 10th proximo.  |     |

- (h) Consumers' net is the published list price less discount shown in the current discount sheets.

4. Commission as described under Paragraph 3 will be paid Vickery, except if in the course of business it is desirable and necessary to cooperate with, enlist the aid of or work with (in sales and service) other sales representative of Fisher to effectuate a particular authorized sale then the commission will be subject to final equitable apportionment between Vickery and such other Fisher representative by Fisher and will be divided on the following basis:

- (1) Purchase Credit —  $\frac{1}{4}$  of assignable commission.  
(Purchase Credit is defined as that portion of credit due to a representative for work in aiding the procurement of an order, when such order is placed in that representative's territory).
- (2) Engineering — Product Acceptance or Engineering Design Credit —  $\frac{1}{2}$  of assignable commission.

Engineering Credit as assignable under this classification shall take into consideration the following phases of work on the part of sales office and representative.

- (a) Writing of original specifications to include Fisher equipment.
- (b) Detail engineering work with contracting engineers or engineer,
- (c) Product Acceptance of, or request for Fisher products by ultimate user

(The above credits may be apportioned between two or more offices based upon circumstances affecting the orders or material concerned on the specific contract in question. Such distribution is to be determined by Fisher).

- (3) Territory Destination Credit —  $\frac{1}{4}$  of Assignable Commission. Territorial credit is that portion of a credit which is due to Vickery or other Fisher representative into whose territory the equipment is shipped or installed. The credit entails the responsibility of servicing customer or user at point of installation, including service to equipment as may be required.
- (4) Fisher reserves the right, in unusual cases, to justly apportion or re-apportion the division of commission.

5. Payments of commission are subject to the following:

- (A) Commissions previously paid for sales during the effective period of this Agreement on equipment returned within one year after shipment, shall be refunded by Vickery, as provided herein.
- (B) No commission will be payable if Vickery's account with Fisher is past due.
- (C) In the event this Agreement is terminated, orders received from and through Vickery will be accrued to his account up to termination date, except that:
  - (1) Shipments made within 60 days after termination date will be subject to one-half of normal commission.
  - (2) Vickery waives all commission on shipments made later than 60 days after termination.
- (D) In the event this Agreement is terminated 50% of the commissions becoming due and payable after the date of termination will be held for a period of 1 year after such date, for the purpose of protecting Fisher on returned equipment and uncollectible accounts.

6. Vickery agrees:

- (A) To employ sufficient, competent assistance for sales, engineering and service, in the above described territory,
- (B) To endeavor to maintain published resale prices,
- (C) To quote preferential discounts only as recommended by Fisher,
- (D) To abide by such rules, regulations or instructions as may be outlined by Fisher,
- (E) To hold in strict confidence, sales data, sales policies, engineering specifications and all other confidential information of like nature,
- (F) To refrain from selling or offering to sell competitive equipment of any person, firm or corporation, during the term of this Agreement, either directly or indirectly, though Vickery may represent other manufacturers of non-competing equipment with the written approval of Fisher,
- (G) To vest title to all sales data, literature, blue-prints, copies of orders, customer correspondence and the like in the name of Fisher and to deliver all such items to Fisher in the event this Agreement is terminated,
- (H) To make no agreement or contracts purporting to bind Fisher, it being specifically understood and agreed that Vickery is not granted authority to bind Fisher in any manner whatsoever, and that all orders obtained by Vickery for the products sold by Fisher are subject to acceptance of Fisher at its office in Marshalltown, Iowa.

7. This Agreement shall begin on October 1, 1960, and it is the intent of the parties hereto that it shall be for a ten (10) year period to run coincidentally with the royalty agreement executed by the parties hereto on the date hereof but further subject to cancellation as set forth below.

Since all other Fisher sales agreements are currently reviewed and renewed annually, it is the intent of this agreement that it be subject to such annual review and subject to negotiation between the parties, should business conditions warrant such review and negotiation.

In the event of cancellation of the aforesaid royalty agreement between the parties, this Agreement will be cancelled automatically.

This Agreement is entered into in good faith by the parties hereto and, in the event Vickery does not diligently, faithfully and properly perform the duties incumbent upon him as an exclusive Engineering, Selling and Servicing Representative, Fisher may cancel this Agreement upon sixty (60) days written notice to Vickery. Whether Vickery is diligently, faithfully and properly performing his duties as an exclusive representative shall be determined by Fisher, not arbitrarily but in the exercise of reasonable discretion and in pursuance of the good faith hereinabove mentioned.

IN WITNESS WHEREOF, Fisher has caused its name to be hereunto subscribed, by its duly authorized officer, and Vickery has hereunto set his hand and seal, all on the day and year first above written.

FISHER GOVERNOR COMPANY

By /s/ J. W. FISHER

*President.*

/s/ EDGAR HERBERT VICKERY

**Appendix C**

Excerpt from deposition of William Fisher, President of Fisher Governor Company, taken on February 7, 1966, approximately four months after the date of the letter of termination (page 89, line 7—page 98, line 15):

“Q. I will now show you a letter [the letter of termination] from Cartwright, Druker, Ryden and Fagg, by Mr. Ryden to Mr. Vickery dated October 2, 1965. Did you direct Mr. Ryden to write that letter, Mr. Fisher?

A. I was aware of the request to write the letter.

Q. Who made the decision to terminate the contract?

A. Fisher Governor's Company management of which I am a part.

Q. Who would that be?

A. Who called and asked him to write the letter, I don't remember.

Q. When you said Fisher Governor Company management, that consists of a body.

A. Yes, it does. You know who they are.

Q. I would like—

A. The officers of the Company.

Q. The officers of the Company, which would be—

A. Mr. Brockett, Mr. Galvin [Fisher's Executive Vice-President] and I, at least.

Q. Three of you?

A. At least.

Q. Did you discuss the termination with anyone else?

A. It seems to me as Ray was involved.

Q. Ray Engle? [He testified that he was not consulted, see paragraph 1.37 (b)]

A. It would have been Ray Engle if there would have been anyone else.

Q. When was the decision made to terminate the contract?

A. At that time.

Q. In October?

A. On October what, 2nd?

Q. Well, was the decision made on the day this letter was written?

A. It was made approximately that time.

Q. Yes. I understand you and Mr. Galvin were in Europe at that time.

A. We were.

Q. As I understand, Mr. Brockett was apparently in on the discussion and if so, this was by long distance telephone conversation, I assume?

A. The decision was reached at approximately the time of the letter.

Q. If you and Mr. Galvin were in Europe and Mr. Brockett was consulted, obviously—

A. It was a mutual decision. I didn't make the telephone call from Europe to Mr. Ryden, if that is what you mean.

Q. I am trying to determine in the decision which led up to the termination I understand the people who participated in that were you, Mr. Galvin and Mr. Brockett and perhaps Ray Engle. If you and Mr. Galvin were in Europe and Mr. Brockett participated in the decision, how did the two of you communicate?

A. I don't remember. Shall I ask?

Q. Well, if you have no recollection about it—

A. Well, I don't remember whether we talked about that on the telephone or not, to tell you the truth.

Mr. Kearney: I gather you had a continuing communication with the factory while you were away.

Witness: Frequently.

Q. You didn't write any letters to Mr. Brockett and Brockett write back to you concerning the termination, I assume, or did he?

A. At this point we had just left and I don't recall that there had been any communication of that nature. I think Mr. Brockett — you were asking me to assume. I can't do it because I wasn't here on that day.

Q. In any event the termination of the contract had your approval and authorization?

A. Yes, it did.

Q. It was made on or about the date of this letter?

A. It must have been.

Q. The decision was made or wasn't made two years prior?

A. No, it wasn't.

Q. It was made about the same time?

A. Right.

Q. I assume when you and Mr. Galvin and Mr. Brockett were discussing this termination you were aware that the termination of the royalty contract automatically terminated the sales contract, isn't that correct?

A. That is correct.

\* \* \*

Q. Why was this decision to cancel the contract made, what was your reason for terminating the contract?

A. Well, we felt the original intents as they were set forth had long since diminished.

Q. What do you mean by that?

A. Disappeared, practically. You asked me early and you know the answers. We had no further instructions, directions or participation by Mr. Vickery and had not had for some time.

Q. Had you requested any?

A. Had I?

Q. Yes.

A. I had not.

Q. Did you direct anyone to request his participation?

A. There was correspondence, I believe, sir, but I was not part of the correspondence.

Q. Who in Fisher Governor Company would have initiated that correspondence, if you know?

A. Any one of the individuals who are involved might have.

Q. Well, who?

Mr. Kearney: Your question is a little bit leading in that you assume that Fisher Governor had to request Mr. Vickery to participate when he has an affirmative duty under the contract to provide additional patents and so on.

A. Anyway that is the way we interpreted it, sir.

Q. Did anyone in the Fisher management to your knowledge ever complain to Mr. Vickery that he was not living up to his side of the bargain under these contracts?

A. Did they complain to him?

Q. Yes.

A. We discussed it that he had not.

Q. Who is we?

A. Mr. Brockett and I.

Q. What specifically didn't he do that prompted this termination?

A. He didn't participate.

Q. In what sense?

A. All the original intents.

Q. There must have been some specific reason.

A. Those are.

Q. He didn't do this or some other thing?

A. He hadn't done them for some time.

Q. Had anyone requested him to do anything?

A. I assume that was part of our bargain that he proffer and pursue it himself.

Q. I want to ask you this question again. To your knowledge did either you or anyone else—

A. I did not.

Q. In Fisher Governor Company complain to Mr. Vickery that he was not offering advice or doing anything else that he was obligated to under the contract?

A. I did not.

Q. Do you know of anyone else who did?

A. Not from first hand experience, I do not.

Q. You stated that Mr. Brockett had some complaints about Mr. Vickery's performance under the contract. What did Mr. Brockett say to you in the way of these complaints?

A. The same thing I just said to you.

Q. In those terms?

A. Do you want me to quote him verbatim?

Q. If you can.

A. I can't.

Q. Give me the substance of it.

A. I did.

Mr. Kearney: I was making a point of distinction. As I gather from Mr. Fisher's answers at the end of this period they reappraised what contribution Mr. Vickery was making rather than specifically requesting. They evaluated his overall performance.

Q. Did anyone else other than Mr. Brockett complain to you about Mr. Vickery's lack of performance?

A. Well, Mr. Allison, my contact is with Mr. Brockett almost altogether.

Q. You didn't talk to Ray Engle?

A. About what?

Q. About Mr. Vickery's performance or lack of it.

A. Yes, but not to the extent that Mr. Brockett and I did discuss it.

Q. Mr. Brockett is Vice President of the sales, is he not?

A. Yes, he is, with direct and frequent contact with Mr. Engle.

Q. Yes. Did you discuss this with Mr. Engle?

A. Briefly.

Q. Mr. Vickery's lack of performance?

A. Yes, sir.

Q. What did Mr. Engle say?

A. Same thing.

Q. Can you give me the substance of what he said?

A. I wouldn't like to quote verbatim.

Q. Could you —

A. The substance is the same.

Q. What is that?

A. Lack of interest, participation and also a lack—by the way a lack of sales which constitutes another business reason of the governmental ball valve.

Q. A lack of sales?

A. Well, I think there was a lack of sales.

Q. You were making a profit on the sales that were made, however?

A. You said so.

Q. Isn't that a fact?

A. I don't know. I told you that before.

Q. Well Mr. Fisher, you were aware, were you not, that there was a profit being made, without tying you to specific numbers? You were aware in general at the time you made the decision to cancel this contract of that?

A. That there was a profit being made?

Q. That there was a profit being made.

A. I don't recall, no, sir.

Q. You had frequent conferences with Mr. Brockett, didn't you?

A. On that particular subject we had some conferences on it.

Q. Didn't he tell you that there was a profit being made?

A. I just told you I don't remember.

Q. Well, to summarize this then, and I would like to have you listen to this summary carefully, the reason for you terminating this contract was because Mr. Vickery didn't show any interest in this program and didn't participate in it, is that correct?

A. That is correct.

Mr. Kearney: And not making any contributions. He listed that.

Q. And not making contributions?

A. He was not.

Mr. Kearney: And lack of —

A. And lack of sales.

Mr. Allison: Just a minute, Counsel.

Q. And a lack of sales in the governmental ball sales program?

A. Yes sir.

Q. Were there any other reasons?

A. Not that I can recall.

Q. Do you think there were any other reasons?

A. No, sir, I don't. I think those are sufficient, by the way.

Q. There was no prior notice to Mr. Vickery of your intention to cancel this contract, was there?

A. Well, I wouldn't think so.

Q. As a matter of fact was there?

A. I don't think so."

## *Appendix D*

Excerpt from deposition of Glenn Brockett, Vice President for Sales of Fisher Governor Company, taken on February 9, 1966, approximately four months after the date of the letter of termination (page 30, line 19—page 34, line 9):

"Q. Now, Mr. Brockett, you were present during the time that Mr. Fisher gave his deposition, were you not?

A. Yes, sir.

Q. You heard him testify that he and Millard Galvin [Fisher's Executive Vice President] consulted with you with respect to the proposed cancellation of the Vickery contract, is that correct?

A. Yes, sir.

Q. And I take it that was a true statement, accurate statement?

A. Yes.

Q. What was the subject of that consultation, or whatever you want to call it?

A. Well, we discussed, of course, whether or not we should cancel it, the contract.

Q. Where were the three parties at that time? I understand Mr. Galvin and Mr. Fisher were in Europe.

Mr. Kearney: You are assuming something.

Q. Would you tell me?

A. Do you want me to tell you what actually happened?

Q. Please.

A. Mr. Fisher did not remember correctly as to these dates and what actually happened. This conversation, I believe, took place in July, in late July.

Q. 1965?

A. '65, yes.

Q. Go on.

A. It was prompted by the reminder from Mr. Walker Allen who is custodian of our contract files that the time of termination of the contract if we wanted to terminate the first five years was approaching. It was his duty to review all contracts periodically and take any action that would be necessary or remind others to do so. So he reminded Mr. Fisher and Mr. Galvin, I presume, that the time was now if we wanted to do it. So Mr. Fisher and Mr. Galvin, and, I believe, Mr. Walker Allen, probably discussed whether or not it would be to Fisher's best advantage to cancel the contract or let it continue. *It was the consensus of opinion that it would be to the best advantage of Fisher Governor Company to cancel the contract.* [Emphasis Added]

Mr. Walker Allen was instructed to discuss this with the attorneys, which he did. They recommended that it not be cancelled in anticipation of the sixty day requirement but wait until the actual date or later of the termination date and then cancel it, making the cancellation effective sixty days after that.

Q. What was the purpose of that recommendation?

Mr. Ryden: Just a minute.

Mr. Kearney: I don't want —

The Witness: That is something I would not know. That was the attorney's opinion, not mine.

Q. I assume that you and Mr. Galvin and Mr. Fisher were all in the same room?

A. Yes.

Q. Tell me what was said by each of the parties to the best of your recollection.

A. I believe that I advised them that in my opinion the volume that we would get in the future based on the actual past history of the deterioration of the market for these types of valves and the fact that Mr. Vickery himself had told me that he didn't anticipate any major use or any incoming large orders as a result of the construction of these new test stands that probably the volume would not be real substantial in the future and that since we were no longer getting any technical help from Mr. Vickery I didn't see that he was performing any useful service to us other than as our sales representative and I could see no reason why we should continue with the royalty contract.

Q. Are you aware of the terms or were you at that time aware of the terms of the royalty contract?

A. Yes, sir.

Q. You were aware that after the first five years there was no longer a minimum royalty payable?

A. Yes, sir.

Q. So if there was nothing sold there was nothing due him, isn't that correct?

A. Yes, sir.

Q. What did Mr. Galvin have to say about this?

A. I don't know that he expressed any opinions to the contrary. I don't remember exactly what either one of them said.

Q. Do you recall what Mr. Fisher said?

A. Mr. Fisher agreed with me entirely and thought this is what we should do.

Q. Would it be a fair statement to say then that the contract was cancelled on your recommendation?

A. I don't know that I would say that exactly. Mr. Fisher was the only one of us who had the authority to tell that it be cancelled. However, I did recommend to Mr. Fisher that it be cancelled and Mr. Fisher was the one."



**United States Court of Appeals  
For the Ninth Circuit**

---

L. B. FOSTER COMPANY, INC.  
*Appellant,*

*vs.*

MELVIN HURNBLAD, and GRACE HURNBLAD, his wife,  
*Appellees.*

---

**APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION**

---

**APPELLANT'S OPENING BRIEF**

---

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FILED

JUN 6 1968



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**United States Court of Appeals  
For the Ninth Circuit**

## L. B. FOSTER COMPANY, INC.

*Appellant,*

vs.

MELVIN HURNBLAD, and GRACE  
HURNBLAD, his wife.

### *Appellees.*

No. 22597

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION

**APPELLANT'S OPENING BRIEF**

## JURISDICTION

This is an appeal from the entry of judgment in favor of the plaintiff in a diversity-tort action (R. 181)\* and from the denial of the motions for judgment notwithstanding the verdict and for a new trial (R. 188). The District Court had jurisdiction under 28 U.S.C.A. § 1332 as this was an action by plaintiffs, who are Washington citizens against Sim Knight, L. B. McGowan, Transport Supply Company, L. B. Foster Company, Inc., and David Paul's Eastport Dodge, Inc., who are all citizens of other states, and the amount of the controversy was in excess of \$10,000 (R. 112-113). This Court has jurisdiction under 28 U.S.C.A. § 1291.

\*Parenthetical references preceded by "R." are to the record. All other parenthetical references, unless otherwise indicated, are to the transcript of the testimony.

## STATEMENT OF THE CASE

### A. The Nature of the Controversy

This action arose out of an accident occurring on December 9, 1963, in Tacoma, Washington, between an automobile operated by the respondents and a semi trailer-truck owned by Sim Knight and L. B. McGowan (defendants herein and hereafter referred to as Knight and McGowan) and operated by Sim Knight. Knight's brakes failed and he ran a red light, striking the respondents.

Events giving rise to this action began to coalesce about the first of August, 1963. It was at that time that Dodge City, Inc., (whose name is now David Paul's Eastport Dodge, Inc., a defendant herein), a Portland, Oregon car and truck dealer, had in its possession a 1946 Peterbilt tractor and a Pointer Willamette trailer. The brakes on the tractor were found to be wanting and Mr. Ross McCullough, a mechanic at Dodge City, relined the rear brakes on the rear axle of the tractor and turned the drums (579). During August, 1963, Knight and McGowan came in to Dodge City, Inc. looking for a truck. On September 5, 1963, Mr. Billie Founal sold Knight and McGowan the Peterbilt tractor and the Pointer Willamette trailer (608).

Knight and McGowan then became engaged in the business of hauling hay from Madras, Oregon, to Tillamook, Oregon (410). This continued over several months until the Tillamook dairymen went on strike and eliminated the truckers' buyers (414). Knight then began to look for someone else for whom he could haul. He was put in contact with the other principal de-

fendant, Transport Supply Company. He contacted by telephone a Mr. Onthanks, who set him up to haul a load of shakes from Portland to Sacramento (338). This was in early December, 1963. Having delivered the shakes, he called Mr. Onthanks from Sacramento whereupon he was advised to go to San Leandro to The Bigge Drayage Co. yard (355-360). These two phone calls were the extent of Knight's contact with Transport Supply Company before the accident (339, 355).

The additional defendant and appellant, L. B. Foster Company, Inc., (hereinafter referred to as Foster), a steel warehousing and fabricating company, received a call in late November, 1963, from Traylor-Pamco of Bellevue, Washington (516). Traylor-Pamco wanted 200 lengths of used railroad rails together with 400 splicing bars for the rail. The sale was arranged by Mr. Felix Baker, a salesman for Foster. Terms required that Foster arrange the transportation and prepay the freight. Mr. Baker was unable to get his usual carrier, Mitchell Bros. Trucking Company (517). At about this time, Transport Supply called Baker and said that they had a truck in the area and inquired as to whether Foster had any business to send their way (517). Baker said they did need a truck and told them where to pick up the shipment of steel (517). Transport Supply had picked up loads from Foster on two previous occasions, November 24, 1963, and December 3, 1963 (276 & 277) and billed for them on December 14, 1963 (278) and December 7, 1963 (524), respectively. These were received by Foster after the shipment in question.

Thus, on December 7, 1963, Knight pulled his truck

into the San Leandro supply yard. The San Leandro yard was owned by the Bigge Drayage Company. Foster leased a storage space in this yard from the Bigge Drayage Company (444). Foster had two employees at the yard, a watchman, Mr. Charles Shewalter, and a clerk-telephone operator, Mr. F. Connors (475). The steel rail was loaded on the trailer under the direction of the driver, Knight, by employees of the Bigge Drayage Company. After having been loaded to his satisfaction, Knight took his truck and headed for Seattle.

Knight spent the night of December 8, in Portland. He took off early the morning of December 9 to complete his trip to Seattle (364). While coming down Wakefield Drive in Tacoma at about 8:00 A.M. that morning, the brakes on Knight's truck-trailer combination failed (367). He proceeded down Wakefield Drive to the intersection of Pacific Avenue. He managed to make a left turn through a red light at the intersection, and then proceeded one block into the intersection of 25th and Pacific Avenues. It was at this point that Mr. and Mrs. Hurnblad, the plaintiffs, came in contact with Knight. They were proceeding through the intersection on 25th Avenue. Knight's truck collided with the passenger's side of the Hurnblad station wagon.

Respondents brought suit against Knight and McGowan, Transport Supply, the company which had contracted with Knight to haul the steel rails, and Dodge City, Inc., now called David Paul's Eastport Dodge, Inc., who sold the truck to Knight and McGowan. In addition, he brought suit against the shipper of the goods, Foster, which had contracted with Transport Supply who in turn had contracted

with Knight, the driver and owner of the truck.

On page six of the pre-trial order, (R. 117), the four allegations of negligence against Foster are set forth. The allegations are:

1. That defendant Foster failed to use reasonable care to employ a careful and competent contractor to do the work which involved a risk of physical harm unless it was carefully and skillfully done.
2. Defendant Foster negligently loaded the trailer in question.
3. Defendant Foster negligently overloaded the tractor in question with a commodity that it was no designed to carry.
4. Defendant Foster violated the provisions of the Motor Carrier Act. 49 U.S.C.A. § 322(c).

Plaintiff's first witness, Mr. James T. Connor, of the Pacific Inland Tariff Bureau, gave most of his testimony over the continuous objection of the defendants (17, 18, 20, 32). He testified that the charge made by Transport Supply to Foster was below that which could be charged by any carrier he knew of (20, 23, 27, 31), that Transport Supply could not make a profit if these were round trips (32), and that the invoice sent to Foster by Transport Supply would put him on notice that something was amiss (49-50) to which defendant again objected (49, 50).

Plaintiff called Mr. Richard Davidson of the Tacoma Police Department, who related what he saw at the accident scene. He also testified that Knight told him he lost his air coming down the hill (92),

that he had been driving truck for 18 years (95), and that this was his first bad accident (95).

Plaintiff called Mr. Jack L. Stewart of the Willamette Tariff Bureau. He testified (270) over objection (269) as to the margin of profits of motor carriers. He also testified that he knew of no motor carrier who could haul for what Transport Supply was charging (277), 280, 285, 287, 288, 289) to which defendant objected (269, 291). And he testified that Transport Supply could not be making any profit on the runs (278, 282, 285) to which defendant objected (269, 291).

The plaintiff then offered the deposition of Mr. Sim Knight. He testified that he had no previous dealings with Foster (332); that he had been a truck driver since 1946 (330); that he had been in no prior accidents nor received any serious tickets (337). He testified that he contacted Transport Supply when he heard they needed drivers with trucks (339). He stated he went to the San Leandro yard after a telephone conversation with Transport Supply (355-56). He testified that he came up over the Siskiyou Mountains without any trouble (374-5), but that coming down the hill in Tacoma his brakes did not hold (367). Knight did not have a certificate or permit from the Interstate Commerce Commission to make the haul in question.

Plaintiff next offered the desposition of Mr. Edwin Cusick, the manager of the Trucking Division of Bigge Drayage Company. He testified to what he would look for on a vehicle he was leasing (453-56) to which defendant objected (453, 456). He also testi-

fied that the shipper has no control over the driver (466).

Plaintiff next offered the desposition of Mr. Harold Gordon, Regional Manager of Foster. He testified that they made no differentiation between new or old carriers (482); that it was common to receive calls from carriers soliciting business (484), and that they take for granted that the carriers are licensed (488).

Plaintiff next called Mr. Felix Baker. He testified that he made the sale to Traylor-Pamco, but when he could not get his regular carrier, he gave it to Transport Supply (517). He testified he did not ask the rate, only when the rails would be delivered (534).

Plaintiff next offered the deposition of Robert Logan. He testified that the price quoted by a salesman depended on how much profit that salesman wanted to make on that sale (541).

Plaintiff next offered the deposition of Charles Whitacre. He testified that he would inquire about a rate only if his sale had a thin profit (548); that the most important thing about a carrier is whether they can pick up and deliver the material.

Plaintiff next called Mr. Kenneth Beadle, Vice President of Pacific Intermountain Express. He testified that shippers do not tell carriers what kind of equipment to buy, nor what drivers to hire (564).

The retired Regional Manager of the ICC for Idaho, Washington and Oregon, Frank Landsburg, was plaintiff's next witness. He testified about a problem with uncertified motor carriers (643) which he said was common knowledge (646) that led to eco-

nomic dislocation because of price-cutting to which defendant objected (643, 644, 645).

At the conclusion of the seven day trial, the jury brought in their verdict. In answer to specific interrogatories, they found that Foster was negligent in the selection of Transport Supply as an independent contractor for interstate transportation of the cargo of steel, and that this negligence was a proximate cause of the injury complained of (R. 180). In addition, they found that there was no overloading or improper loading of the vehicle. Further, they found that Foster had violated Section 322(c) of the Interstate Commerce Act and this violation was negligence and that this negligence was a proximate cause of the injuries involved (R. 180). The jury found damages for plaintiff Melvin Hurnblad in the amount of \$12,500 and damages for plaintiff Grace Hurnblad in the amount of \$62,500 (R. 176). The jury also brought in a verdict against defendants Knight and McGowan and a verdict for defendant David Paul's Eastport Dodge (R. 176). The additional defendant Foster then moved for a judgment notwithstanding the verdict and/or in the alternative for a new trial (R. 183). This was denied by the court (R. 188). Additional defendant Foster then filed notice of appeal to this Court (R. 190).

## B. Questions Involved

1. Where a shipper contracts to have his goods carried by a carrier who in turn contracts a trucker to do the job, can the shipper be held liable for the negligence of the trucker?
2. Can a shipper be held liable for negligence in em-

ploying an independent contractor when there is no evidence that this independent contractor was incompetent?

3. Where there is no showing of incompetence of an independent contractor at the trial, can it still be said that the shipper should have known he was incompetent?

4. When the shipper's only contact with the trucker was when the trucker pulled his truck into a storage yard operated by another trucking firm, can it be said that the shipper should have known that the trucker was uncertified?

5. When the only bills from the carrier arrived after the shipment in question was on its way, can it be said that the shipper should have known that the rates were below the allowed minimum?

6. Can a plaintiff claim the violation of a statute is negligence *per se* when plaintiff is not within the group to be protected by the statute, and the harm suffered is not that which the statute was intended to remedy?

7. Can violation of a statute, by shipping on an uncertified carrier, be the proximate cause of an accident which was actually caused by the truck driver's negligence in failing to check his brakes while on the road?

8. Is not the admission of repetitive irrelevant testimony concerning the minimum legal rates of certified carriers so erroneous and prejudicial as to be reversible error?

9. Is not the admission of testimony as to what procedure would be followed by an ICC certified carrier when he leases a truck reversible error when the court, in failing to strike the irrelevant testimony instead instructs the jury that they can use it in any way they want?

10. Is not the admission of prejudicial testimony concerning the reputation and activities of the class of uncertified carriers reversible error when the only issue is the reputation and activities of a particular carrier?

11. Can a substantial verdict for plaintiff stand when the court has erroneously instructed on proximate cause?

12. Is it not reversible error to instruct that statutes and regulations, which are applicable only to carriers, should be considered in determining a shipper's liability, particularly when the court refuses to instruct that the shipper has no duty to enforce the statutes and regulations?

13. Is it not reversible error to instruct on plaintiff's theories of the case when he has failed to introduce substantial evidence to support any of his theories?

## SPECIFICATIONS OF ERRORS

1. The denial of additional defendant's motion to dismiss plaintiff's complaint for insufficiency of the evidence (856-57).

2. The denial of additional defendant's motion for judgment notwithstanding the verdict (R. 183 and 188).
3. The denial of additional defendant's motion for a new trial (R. 183 and 188).
4. The court's charge as to Foster's liability for employment of an independent contractor (889-890) (R. 163, 164).

In general, no person is liable for the negligent acts of an independent contractor committed in the performance of his contract work. However, one who engaged an independent contractor has the duty to use reasonable care to employ a competent and careful contractor when the work required of such contractor involves a substantial or serious risk of personal injury to third persons unless such work is performed with reasonable skill and care. Failure of Foster Company to use ordinary and reasonable care in selecting a reasonably careful and skillful contractor would constitute negligence and would warrant a recovery by plaintiffs against the defendant Foster Company provided the jury also finds it established by a fair preponderance of the evidence that such negligence proximately caused or proximately contributed to causing the collision in question.

The words "competent and careful contractor" mean a contractor who has available safe and adequate equipment and who possesses the knowledge, skill and experience which a reasonably prudent person in the same or similar circumstances would consider necessary for performance of the contract work without creating an unreasonable and serious risk of injury to the person and property of others.

In determining whether Foster Company employees exercised reasonable and ordinary care in engaging as its independent contractor the Transport Supply Company, and the equipment and driver it might provide, you should consider the care which a reasonable prudent person would use under the same or similar circumstances, including but not limited to the following factors:

1. The danger to which others will be exposed if adequate and safe equipment is not used or the contractor's work is not properly and safely done.
2. The character or nature of the contracted work, that is, whether the work requires only ordinary competence or is work which can be properly done only by special equipment operated by persons possessing some special training, skill and experience.
3. Whether or not the independent contractor selected for carrying the shipment is reasonably qualified to perform the work without unreasonable and unnecessary risk of injury to other users of public highways.

to which additional defendants objected (915):

We take exception to the Court's discussion of either of the three grounds of recovery enumerated in the Court's instructions against the Foster Company, and I take it is not necessary for me to spell those out?

THE COURT: No, I have them right here.

MR. MOCERI: For the reason that there is no evidence on either of these three grounds that either ground was the proximate cause of the accident, and I will not spell that out in detail. We have previously presented that to the Court and I am sure that the Court is fully aware of the contentions that we have been making here.

simply to add —

THE COURT: You have continuously contend-ed right from the beginning that the matter of rates, ICC regulations, and the like, and all mat-ters pertaining thereto is not a proper basis for recovery, and there is no evidence to show they were the proximate cause related to the collision in question. So there is no need of repeating that.

MR. MOCERI: With reference to the grounds of negligence and selection of an independent contractor, we would as an additional ground urge with reference to that that there is no evi-dence that Transport Supply Company, which was the contractor which we engaged, had any equipment deficiency or personnel deficiency or any propensity or deficiency or proclivity, which was a proximate cause or reasonably related to the cause of the accident herein.

5. The refusal of additional defendant's requested instruction No. 23 (R. 60):

You are instructed that there is no evidence that L. B. Foster Company was negligent in the selection of Transport Supply Company as a carrier to deliver the load in question, and that issue is removed from your consideration.

No. 4 (R. 41):

You are instructed that there is no evidence that L. B. Foster Company had any knowledge that Transport Supply Company was not a com-petent carrier of the goods in question. There-fore, it cannot be held for any incompetence, if any, of Transport Supply Company, nor for any incompetence, if any, of Sim Knight, the trucker engaged by Transport Supply Company.

No. 20 (R. 57):

You are instructed that L. B. Foster Company had no duty to inspect the braking system of the truck operated by Sim Knight at the time of the accident and that issue is removed from your consideration.

No. 21 (R. 58):

You are instructed that L. B. Foster Company had no duty to inquire to determine whether Transport Supply Company and/or Sim Knight had complied with the Interstate Commerce Act, or any rules and regulations of the Interstate Commerce Commission and that issue is removed from your consideration.

to which the additional defendant objected (918):

Those instructions, Your Honor, relate to the same issues of sufficiency of the evidence to create a jury question on proximate cause or on negligence which we have previously discussed, and I will not go into more detail.

6. The refusal of additional defendant's requested instruction No. 9 (R. 46):

You are instructed that L. B. Foster Company selected Transport Supply Company to haul the load in question. However, there is no evidence of any negligence in the selection of Transport Supply Company.

You are instructed that L. B. Foster Company did not select Sim Knight as carrier of the haul in question, but rather Sim Knight was selected by Transport Supply Company. Therefore, you are instructed that L. B. Foster Company cannot be held responsible for any negligence in the selection of Sim Knight as the trucker of the haul in question.

and the grounds upon which it was urged (919):

We except to the Court's failure to give defendant's requested instruction number 9, Your Honor, and particularly the last sentence where the jury would be advised that L. B. Foster Company cannot be responsible for any negligence in the selection of Sim Knight as the trucker of the haul in question for the reason that we do not participate in that selection, and they might conclude that he was a negligently selected trucker, and this sentence would advise them that we are not responsible for that.

7. The refusal of additional defendant's requested instruction No. 11 (R. 48) :

You are instructed that the defendants Sim Knight and L. B. McGowan were independent contractors as far as their relationship to L. B. Foster Company is concerned, and L. B. Foster Company is not liable for any negligence of Sim Knight and L. B. McGowan.

and the grounds upon which it was urged (919) :

We except to the failure of the Court to give requested instruction number 11 wherein the jury would be advised that Sim Knight and L. B. McGowan were independent contractors as far as their relationship to L. B. Foster Company is concerned and we cannot be held liable for their negligence.

The Court did instruct the jury that you are not liable for negligence as an independent contractor and does not specifically refer to those two defendants.

8. The admission into evidence of testimony relating to the procedure followed by an ICC licensee when leasing equipment (454) :

Q. If a truck at that time would have called at

the Bigge yard to haul for Bigge Drayage without such marking what would have been the position of Bigge Drayage concerning such equipment.

- A. Well, there's a ritual that you go through. You physically check the mechanical condition of the equipment. There is a compliance sheet that you have to fill out. The placards have a specific number and they are registered as such and then you check to make sure the driver has had a valid ICC physical, and in our particular case they would have to go on our payroll if they were used for less than 30 days and just follow the full procedures of the safety regulations of the Interstate Commerce Commission.

to which the additional defendant objected (456):

MR. MOCERI: Now, Your Honor, I move this testimony be stricken because it is now clear he was referring to their leasing operation.

THE COURT: The testimony, as the jury will note, apparently refers to an occasion when an ICC permittee leases equipment and perhaps personnel to operate it from someone else. There is no suggestion here that a leasing was involved in this case, but if you find that that procedure described here has some other bearing in another way to the issues in the present case, you may treat it so, otherwise, not.

Of course, you will receive instructions concerning the issues in this case at a later time. Then you may make a determination as to whether or not this is applicable or not, whether it has probative value or not to the issues that you are to consider.

9. The admission into evidence of testimony regarding the reputation of the group of unlicensed

motor carriers (643):

Q. All right. In your experience with the Interstate Commerce Commission did you become aware with a problem involving non-licensed or unregulated highway motor carriers?

A. Yes.

Q. (By Mr. Hulscher) In your experience with the Interstate Commerce Commission and your activities in the safety field, did you become aware of a problem involving unlicensed or unregulated highway motor carriers?

A. Yes sir. It was necessary for us to work with that problem consistently.

Q. (By Mr. Hulscher) In the year 1963, sir, was there a general reputation in the industry among carriers — highway carriers, shippers, and regulatory agencies concerning certified or unregulated carriers operating in interstate commerce?

A. Yes, sir.

to which the defendant objected (643):

MR. RUTHERFORD: I would object, Your Honor, to testimony on that point because proof of what some other group or people do is no proof of what another does at a specific time and place.

THE COURT: I think in view of the jurisdiction of the office of which Mr. Landsburg was in charge and the particular question now put, you may certainly answer that at a minimum. Go ahead.

(page 644):

MR. RUTHERFORD: Here again I would object.

THE COURT: First of all, I think you better

state with what the problem was, then we will decide from there.

MR. RUTHERFORD: I would object on the grounds of relevancy.

THE COURT: I think not. I think it is relevant.

MR. RUTHERFORD: Any law enforcement agency has problems, and that doesn't mean that some specific individual —

THE COURT: I can't tell what he is talking about until he states what the problem is, and when he states that, we will consider it in the light of that.

You may state what the problem was, Mr. Landsburg, please.

MR. HULSCHER: May I withdraw that question and ask another so that we can lay a proper foundation?

THE COURT: Yes, you may.

(Page 645)

MR. RUTHERFORD: It is necessary for me to reiterate my objection to this last question?

THE COURT: No, it is not. The same objection will be applicable wherever appropriate to the text.

MR. MOCERI: I might say the question is different. He is talking about reputation rather than a problem, and I guess he is going to try and prove a reputation of one person by the reputation of a class, which is not proper.

THE COURT: The word "reputation" is a little questionable in that context. Would you please clarify what you mean by that?

MR. HULSCHER: For the record, Your Honor, I am not offering reputation to prove the

truth or falsity of the reputation. I am offering the reputation to prove the knowledge of shippers in the industry.

THE COURT: I understand that. The only difficulty from my point of view is that I think there would be a better word to use rather than "reputation."

to which additional defendant objected further (856) :

We would further move that the testimony of the witness Mr. Landsburg, who was from the Interstate Commerce Commission, a former representative of the ICC, be stricken from the record for the reason that it is improper to show the propensities or characteristics of a person of a class specifically and simply by testifying to the general characteristics of a class of which that person is a member. This being a tort action, we would contend that the plaintiff has to prove the characteristics or propensities of this carrier by —of which there is no evidence that this carrier and Transport Supply Company had any defective equipment or had a reputation for having incompetent drivers or inability to not maintain their equipment, and we, therefore, move the testimony relating to the negligence selection of Transport Supply Company be stricken and that issue be withdrawn from the jury's consideration.

10. The Court's charge as to Foster's liability for violation of Section 322(c) (888) (R. 166-167) :

The third ground of recovery asserted by plaintiffs against the defendant Foster Company is based on a violation of the Federal Interstate Commerce Act. This law of the United States provides it shall be unlawful for:

"any shipper, or any officer or employee thereof [to] knowingly accept or receive any [rate] concession in violation of any provision of the

[Interstate Commission Act].”

For convenience, this section of the law will be referred to as “Section 322.”

One of the purposes of the Interstate Commerce Act and of Section 322 is to regulate and supervise vehicles engaged in interstate commerce on public highways and to provide for the safety of such vehicles and all users of public highways. To this end, Congress has provided that no person shall engage in any for-hire transportation by motor vehicle in interstate commerce on any public highway “unless there is in force with respect to such person a certificate or a permit issued by the [Interstate Commerce] Commission authorizing such transportation.”

Under the evidence it is an undisputed fact that defendant Sim Knight was not a driver authorized to transport commodities in interstate commerce under a certificate or permit of the Interstate Commerce Commission at the time he performed the interstate transportation of the load of steel in question.

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If you find it has been established by a fair preponderance of the evidence that employees of Foster Company at or prior to the time the cargo of steel in question was loaded at San Leandro, California for interstate shipment to the State of Washington knew, or in the exercise of reasonable care should have known:

1. That the defendant Knight did not hold a valid certificate or permit issued by the Interstate Commerce Commission authorizing Knight or his vehicle to perform interstate transportation of the shipment, and

2. That the amount of charges by Transport Supply Company to Foster Company for such interstate transportation was less than the minimum rate Foster Company would have been re-

quired to pay for such transportation by a carrier, which was certified by the Interstate Commerce Commission, then you may find that Foster Company, as a shipper, violated the above stated provision of Federal Law, Section 322, and such violation, if you find it occurred, would constitute negligence as a matter of law.

As previously stated, however, a violation of Section 322 and consequent negligence of Foster Company in that particular standing alone is not sufficient to find Defendant Foster Company liable to the plaintiff. It must be also shown by a fair preponderance of the evidence that the violation of Section 322 by Foster Company proximately caused or contributed to causing the collision involved in this case.

to which additional defendant objected as to the giving (915):

MR. MOCERI: For the reason that there is no evidence on either of these three grounds that either ground was the proximate cause of the accident, and I will not spell that out in detail. We have previously presented that to the Court, and I am sure that the Court is fully aware of the contentions that we have been making here simply to add —

THE COURT: You have continuously contended right from the beginning that the matter of rates, ICC regulations, and the like, and all matters pertaining thereto is not a proper basis for recovery, and there is no evidence to show they were the proximate cause related to the collision in question. So there is no need of repeating that.

and as to the form (917):

Now, further with reference to the third ground of recovery, we take exception to the

portion of the Court's instruction wherein the Court advises the jury as follows, "If you find," and I am now quoting from the last paragraph, "if you find that established by a fair preponderance of the evidence that employees of Foster Company at or prior to the time the cargo of steel in question was loaded at San Leandro, California for interstate shipment to the State of Washington knew, or in the exercise of reasonable care should have known," we take exception to the "or in the exercise of reasonable care should have known."

That instruction advises the jury that there can be a violation of this statute without actual knowledge but only if they should have known, and we submit that to violate this statute, the "knowingly" means that knowingly and that it has to be based on actual knowledge and it has to be based on a finding of actual knowledge, which, of course, can be gathered from all the circumstances but it cannot be based on a finding that they should have known, and we submit that this is an erroneous interpretation of the statute.

11. The refusal of additional defendant's requested instruction No. 8 (R. 45) :

You are instructed that the duty to enforce the Interstate Commerce Act pertaining to motor carriers and the rules and regulations of the Interstate Commerce Commission is that of the Interstate Commerce Commission and not upon a shipper such as L. B. Foster Company, Inc.

and the grounds upon which it was urged (919) :

We except to the Court's failure to give instruction number 8 wherein the jury would have been instructed the defendant L. B. Foster Company had no duty to enforce the provisions of

the Interstate Commerce Act and provisions of the rules and regulations thereby. We feel this is particularly significant in light of the Court's instructions advising the jury they may consider these rules and statutes and regulations as against this defendant.

12. The refusal of additional defendant's requested instruction No. 17 (R.54):

You are instructed that whether Transport Supply Company charged L. B. Foster Company a lawful rate for the haul in question, was not a proximate cause of the accident and that issue is removed from your consideration.

No. 18 (R. 55):

You are instructed that whether Transport Supply and/or Sim Knight were licensed by the Interstate Commerce Commission was not a proximate cause of the accident and that issue is removed from your consideration.

No. 19 (R. 56):

You are instructed that L. B. Foster Company had no duty to inquire as to what rate would be charged by Transport Supply Company for the load in question and that issue is removed from your consideration.

No. 22 (R. 59):

You are instructed that L. B. Foster Company had not duty to inquire as to whether Transport Supply Company and /or Sim Knight were licensed by the Interstate Commerce Commission to haul the load in question.

13. Charge of the Court as to proximate cause (875-876) (R. 153):

The term "proximate cause" means that cause which in a direct, unbroken sequence produces the injuries complained of and without which the injuries would not have occurred. One chargeable with negligence is liable for injury which was reasonably foreseeable in the exercise of reasonable care, whether or not such consequence of a negligent act or omission actually was foreseen by the negligent party. If a particular negligent act or omission initiates a series or chain of causation, in which each connecting causative factor is proximately caused by the preceding factor and in turn proximately causes a succeeding factor, and the unbroken sequence finally causes injury or damage, such end result, in law, is chargeable to the negligence which initiated the series or chain of causation.

and the grounds of the objection were (913-14) :

MR. MOCERI: Your Honor, comes now the defendant L. B. Foster Company and excepts to the Court's instructions as follows, first we except to that portion of the Court's instruction on proximate cause reading as follows: [here counsel quoted the Court's instructions as above] for the reason that that statement of the law upon proximate cause goes beyond the concept of proximate cause. The first two sentences of the Court's definition does contain the concept of proximate cause, which includes the concept of foreseeability.

However, the sentence that I have just referred to goes beyond the concept of foreseeability and relies strictly on cause and effect or what is referred to as the "but for" doctrine, which is not the concept of proximate cause.

14. The admission of testimony as to the lawful rate (20) :

Q. Now, were you aware of anyone at the time these shipments were made that could have lawfully hauled the commodity in question for the rate stated on the Transport Supply invoice?

MR. MOCERI: Object, Your Honor —

MR. RUTHERFORD: Object to the form of the question, asking the witness to comment on the law.

THE COURT: Well, if I understand it correctly, it is with their common carriers, the regulated common carriers available for the carriage of this shipment from the point indicated, is that what you are asking?

MR. HULSCHER: At the 90 cent rate, Your Honor.

THE WITNESS: Not of my knowdelge.

And with another witness (272):

Q. Are you aware of any motor carrier in the industry anywhere, including California, Oregon, and Washington that could have lawfully hauled the commodities there for the rate charged by Transport Supply Company?

A. I cannot, sir.

to which defendants objected:

MR. MOCERI: I would make the same objection previously made as to what I anticipate the entire line of inquiry of this witness will be and on the additional grounds that it is repetitious, covering the same ground that another witness previously covered.

15. The admission of testimony as to the minimum rate that would have been charged by carriers which

were members of the Pacific Inland Tariff Bureau (17):

Q. Now sir, would you tell us what the minimum rate would have been for that haul for those carriers you represent?

MR. MOCERI: I object to this line of inquiry, Your Honor, on the grounds that it is irrelevant and immaterial on the issue of proximate cause of the accident between Sim Knight and the plaintiffs.

THE COURT: That contention will be deemed as a continuing contention, and when all of the evidence applicable to that position is before us, I will then rule on it. For now I will admit it, subject, however, to later being stricken.

Ladies and gentlemen, whether this particular phase of the case will become an issue for you to consider will be determined at a later date. In other words, the evidence is now admitted pertaining to this subject matter tentatively, that is, to a determination by the Court after all the evidence pertaining to this issue is presented, whether or not it is sufficient to raise a question for the jury to consider.

Go ahead.

MR. MOCERI: I had another ground here I might state.

THE COURT: Go ahead.

MR. MOCERI: The additional grounds that I had here is that, and I am assuming that counsel is going to go ahead with A through D, is that the dates of these invoices are all after the date of the shipment here, and we would object on the additional grounds without showing any prior knowledge on the part of L. B. Foster Company.

THE COURT: That would be another objection final ruling on which will be made when we

have the whole matter laid before us.

**MR. RUTHERFORD:** The defendants Knight and McGowan also join in the objection on the grounds of relevancy. We don't feel it has any bearing.

**THE COURT:** I might say now, to save time of duplicitous objections, that as far as I'm concerned, if it is agreeable with counsel for the plaintiff and you gentlemen for the defendant, that any objection voiced by the defendant may be deemed as having been joined in by any other defendant to whom the objection would be applicable. That will mean that you will not need to object. On the other hand, if you feel so incensed that you would like to let off a little steam or state some additional ground or the like, of course, you are free to do that.

All right. Go ahead.

**Q.** All right. Now, will you tell us, sir, what the minimum rate would have been for those carriers which you represent for this haul?

**A.** The ICC filed motor carrier tariffs at this date in question was \$3.56 per 100 pounds, LTL, which means less than truckload, which also means would apply on any quantity which is less than a particular stated weight, such as 10,000 pounds. This was reflected in 22 Revised page 330 of Pacific Inland Tariff Bureau, number 9-C bearing an effective date of November 23, 1963.

To which there was the further objection (854):

First of all, Your Honor, relating to the exhibits which relate to rates that were charged by Transport Supply Company to L. B. Foster Company and all of the testimony on the rates that were charged by Transport Supply Company to L. B. Foster Company, we move those exhibits

and that testimony be stricken from the record for the reason that it would not be a proximate cause of the accident herein.

16. Charge of the Court which stated that the statutes and regulations which by their terms affect only motor carriers could be applied to a shipper (880).

The Court instructed the jury on inspection and maintenance requirements of motor carriers, on equipment requirements for vehicles, on standards for motor vehicle operators, on maximum speed limits, and on traffic control signals. After quoting statutes and regulations in detail for two pages (R. 157-158) the Court advised the jury as follows (R. 159):

As previously stated, all of the foregoing statutes and regulations are specifically applicable only to owners and operators of motor vehicles, and violations thereof by defendants Knight and McGowan would constitute negligence on their part as a matter of law.

*However, the safety standards prescribed by such laws and regulations may be considered by the jury along with all other circumstances shown by the evidence in determining whether either defendant Foster Company or defendant Eastport Dodge was negligent in failing to exercise reasonable care in any particular alleged against them, and of so, whether such negligence was a proximate cause of injury or damage to the plaintiffs.*  
(Italics added)

to which the additional defendant objected (914-915):

Second, Your Honor, we will except to that portion of the Court's instruction as follows, this Court's instruction on Sim Knight and McGowan

after the Court quoted these statute and regulations and the Court gave this instruction to which we now except. [Here the additional defendant quoted the italicized portion of the charge set forth above].

We except to that instruction, Your Honor, for the reason that it advised the jury that these regulations, which on their face apply only to motor carriers, may be deemed applicable to the L. B. Foster Company, and which on their face are not applicable, that it does create a misleading inference as to the applicability of these statutes and instructions to the Foster Company.

### SUMMARY OF ARGUMENT

The prime issue presented for determination here is whether a principal can be charged with the negligence of an independent contractor. In this case it is not the independent contractor with whom the principal dealt, but rather another sub-contractor who contracted with the independent contractor. A determination that vicarious liability cannot extend through two independent contracts ends consideration of the case without need to delve into the particular circumstances.

Another issue raised is whether a plaintiff can proceed to the jury on his theory that defendant selected an incompetent independent contractor when plaintiff fails to introduce any evidence of any sort of antecedent activity by the independent contractor which would indicate incompetence.

Another portion of the argument deals with the question of proving negligence and proximate cause based on the violation of statute. The first issue raised

is what minimum amount of evidence must plaintiff introduce when the criminal statute requires a knowing violation. Then, too, can plaintiffs claim benefit of a statute which was not enacted for their benefit nor designed to remedy the harm they sustained? Finally, the issue of what causal connection exists between a shipper shipping on an uncertified carrier and injuries sustained because of an accident resulting from the driver's negligence is discussed.

The last portion of the argument deals with the reasons for which appellants claim the right to a new trial. These relate to (1) admission of irrelevant, prejudicial testimony about "bloody accidents" left by uncertified carriers, (2) admission of irrelevant, confusing testimony about "lawful rates", (3) admission of irrelevant and misleading testimony about what a certified carrier would look for in a trucker, (4) a charge which allows the jury to apply motor carrier statutes and regulations to a shipper, and (5) a charge which sets forth an incorrect definition of proximate cause. Although appellants believe that each of the reasons warrants a new trial, the court is also to consider the cumulative effect of the various reasons.

## ARGUMENT

### I. A PARTY INJURED BY THE NEGLIGENCE OF AN INDEPENDENT CONTRACTOR, WHO HAD A CONTRACT WITH ANOTHER INDEPENDENT CONTRACTOR, WHO HAD A PREVIOUS CONTRACT WITH A THIRD INDEPENDENT CONTRACTOR, HAS NO CLAIM AGAINST THE THIRD INDEPENDENT CONTRACTOR FOR THE NEGLIGENCE OF THE FIRST INDEPENDENT CONTRACTOR

This is the novel question which this case presents. Here the plaintiffs, who were injured in a truck-auto collision, which collision was proximately caused by the negligence of the driver of the truck in failing to properly inspect and repair the truck, sought to obtain recovery not only against the owners and driver of the truck, the dealer who sold them the truck, the carrier with whom the driver contracted to haul, but even the shipper whose goods the driver was delivering.

Transport Supply was an independent contractor with respect to Foster and the jury was so instructed (R. 164). In addition, Knight was an independent contractor in respect to Transport Supply. Knight owned his own truck (333), was self-employed in the trucking business for a number of years (341), did not have a continuing relationship with Transport Supply (339, 355) and was paid not by the hour but by the weight to haul the shakes to California (362). No specific price had been agreed upon for the hauling of the steel rails in question (362). It was never contended at the trial that Knight was not an independent contractor in his relationship with Transport Supply. Under the law of the State of Washington this was clearly the relationship. See *Hollingbery vs. Dunn*, 68 Wn.2d 75, 411 P.2d 431 (1966).

Thus, the question presented by this appeal is can a party injured by the negligent operation of a truck, recover from a third party whose only connection with the accident was that he contracted with an independent contractor (Transport Supply) to have goods delivered to a buyer, and the independent contractor (Transport Supply) in turn contracted with another independent contractor (Knight) to deliver

the goods, which independent contractor picked up the goods and whose subsequent negligence caused the injury. The effort which must be made to get this contention into any kind of understandable grammatical form reveals the significant lack of legal underpinning from which the contention suffers. The hornbooks, the annotations, and the digests are legion with the cases wherein a principal is held not liable for the actions of an independent contractor. Moreover, exhaustive research reveals no case wherein a principal was held liable for the negligent acts of his independent contractor's own independent contractor.

One case in which this untenable proposition was advanced was *DeMichiel v. General Crushed Stone Co.*, 218 F.2d 186 (3 Cir. 1954). The injured party sued the driver and the owner of the truck which injured him. He also sued the alleged principal, the general contractor on the job. The district court granted the general contractor's motion for a judgment N.O.V. The plaintiff appealed. The court affirmed holding that the stone company which subcontracted supplying of stone to another independent contractor who, in turn, contracted with an independent trucker for hauling of stone, was not liable to the person injured due to the negligence of the trucker hired by such independent contractor. The court said that since there was no question from the evidence that the general contractor was at least two independent contractors removed from the individual who was negligent, there was no theory of law under which the jury could find responsibility.

So it is too here. Foster, by its salesman Barker,

made a contract with Transport Supply (517) to have the steel rails delivered to Seattle. Transport Supply then in turn made a contract with the trucker Knight (355) to pick up and deliver the rails. Knight picked up the rails at the San Leandro yard of Bigge Drayage (360) and proceeded toward Seattle. Sometime later while he was on the road he failed to check or failed to properly repair his brakes. This negligence resulted in the truck losing its brakes in Tacoma. This was two days and 800 miles from any contact with Foster. The negligent acts of Knight which caused the harm are too remote in time, space and contractual relationship from Foster to result in any liability to Foster. Thus, the trial court erred in not dismissing Foster as a defendant at the end of the case (856), and in not granting Foster's motion for a judgment notwithstanding the verdict (R. 183 and 188).

## **II. THE EVIDENCE FAILED TO ESTABLISH ANY NEGLIGENCE IN FOSTER'S CONTRACTING WITH TRANSPORT SUPPLY.**

### **A. No showing of incompetence of Transport Supply.**

The jury found that Foster was negligent in selecting Transport Supply as an independent contractor for transportation of the shipment of steel in question. The jury further found that this negligence was a proximate cause of the injury to the plaintiff. Neither finding is supported by the evidence.

The general rule has always been that an employer is not liable for the torts of those with whom he contracts.

This was stated categorically in the case of *Bill v. Gattavara*, 24 Wn.2d 819, 837, 167 P.2d 434 (1946)

Although in some early cases it was thought that the doctrine of *respondeat superior* applied to the relation between an employer and an independent contractor, the authority of these few cases was soon overwhelmed by many decisions promulgating the general rule that *an employer is not liable for the torts of an independent contractor or the latter's servants*. This rule of non-liability of an employer is based upon the theory that the characteristic incident of the relation created by an independent contract is that the employer does not possess the power of controlling the person employed *as to the details of the stipulated work*; and it is therefore, a necessary judicial consequence that the employer shall not be answerable for an injury resulting from the manner in which the details of the work are carried out by the independent contractor.

(Court's emphasis)

See also *Kirk v. United States*, 270 F.2d 110, 116 (9th Cir. 1959) wherein this court referred to this proposition as "the generally applied and well-established rule that a contractee is generally not liable for the torts of an independent contractor or of the latter's servants."

A generally accepted exception to this rule has been carved out. This exception imposes liability on the employer for the harm proximately resulting from failure to select a competent independent contractor. See *Prosser, Torts*, p. 481 (3rd ed. 1964); annotation 8 A.L.R.2d 267 (1949).

The Washington Supreme Court has dealt with the question of the incompetency of a given employee or

contractor on many occasions. The first case to deal squarely with this problem was *Richardson v. Carbon Hill Coal Co.*, 6 Wash. 52, 32 Pac. 1012 (1893). This was an action by an employee against an employer for injuries sustained in a mine and for subsequent negligent treatment from the doctor provided by the company. In the course of its discussion, the court (pp. 56, 57) draws a clear distinction between the doctor being negligent and being incompetent. As to the first, the court points out the evidence which shows how the treatment of this plaintiff-patient was negligent. They then turn to the testimony concerning the doctor's competency. They conclude that it shows he was "grossly incompetent; that is, he was habitually very seriously under the influence of liquor, so as to render him unfit for duty." This case is important not only because it gives an example of incompetency, but because it points out the distinction that must be kept in mind throughout the entire consideration of this case: That is, the distinction between the words "incompetent" and "negligent". In this case, the court clearly shows that negligence refers to the particular act which gave rise to this particular lawsuit; whereas competency or incompetency refers to the characteristics displayed by the individual antecedent to the act involved.

As the Alabama Supreme Court stated succinctly in discussing this problem:

Negligence is not synonymous with incompetency. The most competent may be negligent. But one who is habitually negligent may on that account be incompetent.

*McGorwin v. Howard*, 251 Ala. 204, 36 So.2d 323, 325 (1948).

More light on the problem has been shed by a Washington case of *Green v. Western America Co.*, 30 Wash. 87, 70 Pac. 310 (1902).

This was an action brought by a coal miner against the owner of the mine. One of the allegations alleged negligence on the part of the mine owner in the employment of an incompetent pit boss. The court stated (page 115) :

The presumption is that the master has exercised proper care in the selection of the servant. It is incumbent upon the party charging negligence in this respect to show it by proper evidence. This may be done by showing specific acts of incompetence, and bringing them home to the knowledge of the master or company; or by showing them to be of such a nature, character and frequency that the master in the exercise of due care must have had them brought to his attention.

The court went on to say that it could only be after repeated acts of incompetency by a servant that any question could arise as to the master's knowledge. This case brings out sharply and distinctly the existence of a presumption in favor of the appellant Foster in this case. This presumption places the burden firmly on the plaintiff to come forward with a significant amount of proof in order to overcome this presumption of due care on the part of the principal.

In a number of subsequent cases the Washington Court has adhered to these principles in handling the problem in question: *Dossett v. St. Paul & Tacoma Lumber Co.*, 40 Wash. 276, 82 Pac. 273 (1905), (where the court ruled that two acts of negligence did not establish incompetence); *Johansen v. Pioneer Mining*

*Co.*, 70 Wash. 421, 137 Pac. 1019 (1914), (where testimony of several specific acts of negligence together with a reputation for incompetence of the foreman hired by the defendant was held sufficient to create a jury question); *Miller v. Mohr*, 198 Wash. 619, 89 P.2d 807 (1939), where the court ruled that even if the evidence showed that the employee in question was incompetent, that the matter had no bearing upon the defendant's responsibility unless "in some manner the information had been brought home to appellant[defendant] prior to the accident" (p. 642).

In the case of *Simon v. Hamilton Logging Co.*, 76 Wash. 370, 136 Pac. 361 (1913) the plaintiff attempted to prove that the doctor contracted for by his employer was incompetent, and for this the principal should be liable. He first offered to prove an instance of alleged malpractice occurring six years before the trial. This was refused as being too remote. Plaintiff then attempted to introduce events which occurred after the case arose. These were also refused. The court stated the rule it was applying in this language.

While incompetency cannot, as a rule, be shown by proof of a single act of negligence, it is proper to show repeated acts of carelessness and incompetency . . . as touching the question whether the employer knew or might have known that the servant was incompetent if he had exercised ordinary care in his selection or retention. (*Simon*, supra at page 373)

Further, the court stated the rule (page 374-5):

Specific acts of negligence brought home to a defendant, and reputation, are evidence of the same quality, and an employer cannot be bound unless there is knowledge, express or implied, at a time, when, if acted upon, he could have re-

fused to employ, or, having him employed, discharged the employee so as to prevent the injury.

Here again the court is pointing out the burden which the plaintiff must bear. He must show acts of carelessness and incompetency, antecedent to the event giving rise to the action, and he must prove that these acts could have been brought home to the employer; or he must at least prove that the individual involved had a reputation for incompetency or carelessness and that this reputation of this individual was brought home to the party to be charged. The plaintiff herein has failed to supply the record with even one instance of a specific act of negligence by Transport Supply. Further, the record is equally lacking any testimony or evidence as to the reputation possessed by Transport Supply.

While there was evidence that Knight was not licensed by the Interstate Commerce Commission for the haul in question, there was no evidence concerning whether Transport Supply had the necessary licenses and permits. However, even assuming that Transport Supply was not properly licensed to engage in an interstate haul, this does not constitute evidence of incompetency. This precise problem was before the Texas Court of Civil Appeals in *Moore v. Roberts*, 93 SW2d 236 (Tex. Civ. App. 1936).

There the plaintiff was injured when struck by a truck owned by an independent contractor who had been hired by the defendant to haul lumber and driven by an employee of the independent contractor. There was a directed verdict for defendant and on appeal plaintiff claimed that it was error to direct a verdict against him for there was an issue of fact

as to whether defendant was negligent in selecting his independent contractor. The allegation of negligence was based on the contention that the driver of the truck owned by the independent contractor did not have a chauffeur's license and that neither the driver nor the independent contractor had a permit from the Texas Railroad Commission to haul as a common carrier. In addition, the truck was a 1929 model Chevrolet and evidence was introduced raising the inference that the brakes were not in proper repair at the time of the accident. The court rejected all of these contentions saying that the defendant had the right in absence of any notice to the contrary "to assume that Nicholson [the independent contractor] was not conducting his business in violation of the law." Further, the court stated:

Reasonable diligence would not require Crews [the employer] to see that Nicholson [the independent contractor] had a new truck, nor to have made an examination to determine if the brakes were in proper mechanical condition, and to see that they remained in such condition throughout the performance of the contract. Assuming that evidence is sufficient to warrant a finding that the brakes were out of repair at the time of the accident, and that Nicholson was negligent in this particular, we do not think such fact would convict him generally of being an incompetent contractor. If the contractor is not an incompetent contractor, the degree of care exercised by the employer in his selection is immaterial.  
(page 239)

A recent case which dealt with the question of liability of the principal for the employment of an incompetent independent contractor was *Mooney vs. Stainless, Inc.*, 338 F.2d 127, (6th Cir. 1964 cert. den. 381 U.S. 925). Here the widow sought recovery

against the prime contractor for the negligence of a subcontractor. She alleged that the principal selected an incompetent independent contractor. The trial court entered judgment for the widow. The Sixth Circuit Court of Appeals reversed, and ordered the suit dismissed. The trial court had instructed that the burden was on the plaintiff to prove the defendant guilty of negligence in the selection of an independent contractor. The appellate court approved this and then reviewed what evidence plaintiff had introduced. She had shown that the independent contractor had previously been an employee for some years, that his bid was substantially lower than the others, that his equipment was not as comprehensive as it might have been, and that he was engaged by long distance telephone. The court did not find this too persuasive. It stated (page 132):

Neither was it shown that Wood [independent contractor] had ever before, either as employee or as contractor, been involved in an accident. There is no showing of anything about the previous history of Wood that would have put Stainless [principal] on notice of any incompetence or unfitness on his part, no matter how complete an investigation might have been made by Stainless in advance of engaging him. Though there is an intimation that Wood's equipment was not as extensive as might have been desirable, no evidence was offered by plaintiff as to what extent he was ill-equipped or under-equipped, or as to what minimum equipment it required in the performance of this type of contract.

The court then announced that they were of the opinion that plaintiff had failed to carry her burden of proof and that there was not sufficient evidence of Wood's alleged incompetence to submit to the jury

the question of whether Stainless was negligent in selecting him. For this proposition they cited *Moore*, supra. On a petition for rehearing the court restated its views. In order to avoid any misunderstanding the court stated, (page 136) :

We held that the burden of proof was upon plaintiff to establish that Stainless was negligent in engaging Wood as an independent contractor, rather than upon Stainless to establish that it exercised due care in selecting Wood as the independent contractor. We then proceeded to hold not only that plaintiff failed to carry her burden of proof, but that there was no evidence whatsoever which could have supported a verdict of the jury on this theory, and that the district court therefore erred in submitting plaintiff's second theory to the jury.

~~Turning to plaintiff's case and the testimony contained therein, the following references are all that plaintiff introduced concerning Transport Supply.~~

Turning to plaintiff's case and the testimony presented therein, these were the only references made by plaintiff's witnesses concerning Transport Supply.

1. From the deposition of defendant Sim Knight (338). He testified that Mr Onthanks of Transport Supply had arranged for him to haul a load of shakes from Portland to Sacramento. He had been put in contact with Transport Supply when he was looking for a hauling job. When he had delivered the shakes, Mr. Onthanks told him to pick up the load of steel rails at the San Leandro yard of Bigge Drayage.

2. From the deposition of Edwin Cusick (449). He testified he had never heard of Transport Supply

prior to the trial.

3. From the deposition of Harold R. Gordon (489). He testified that he did not remember dealing with Transport Supply nor did he remember anything about them.

4. From the testimony of Felix Baker (517). He testified he had arranged for Transport Supply to haul the load of steel rails after they called him looking for business. He also testified he had used them once before.

5. From the deposition of Charles Whitacre (546). He testified he had no knowledge whatsoever about Transport Supply.

Plaintiff had the opportunity with Mr. James Connor of the Pacific Inland Tariff Bureau of Seattle (10-58) to inquire as to his knowledge of specific acts of negligence or reputation for incompetence on the part of Transport Supply. He did not do so.

Plaintiff again had the opportunity with Mr. James F. Johnston (101-157). He was sales representative for Pacific Intermountain Express, and knowledgeable of trucking activity in the northwest. Plaintiff did not ask him anything about Transport Supply.

Likewise with Mr. Jack L. Stewart (267-324), whose Willamette Tariff Bureau was based in the same town as Transport Supply, plaintiff did not inquire about Transport Supply's acts or reputation.

He also failed to inquire of Mr. Kenneth Beadle (552-576), a Vice President of Pacific Intermountain Express, as to what the reputation of Transport Supply was.

Finally, Plaintiff had the opportunity with Mr. Frank Landsburg (640-666), retired Regional Manager of the Northwest District of the Interstate Commerce Commission to inquire about Transport Supply's reputation. In all of Mr. Landsburg's testimony, over objection (643-645), concerning the reputation of the class of uncertified carriers, he in no way referred to Transport Supply.

In consideration of the record as a whole, there is simply no evidence to be found anywhere to show either specific acts of negligence or a reputation for negligence on the part of Transport Supply Company. Therefore, without even a scintilla of evidence, much less substantial evidence, to support the conclusion that the independent contractor was incompetent, the jury's finding of negligence cannot be supported by the record.

#### **B. NO SHOWING THAT FOSTER KNEW OR SHOULD HAVE KNOWN THAT TRANSPORT SUPPLY WAS INCOMPETENT.**

This proposition follows immediately from the above argument. If the plaintiff was unable to produce any evidence to show to Foster at the trial that they had in fact contracted with an incompetent, how much less could Foster be expected to know this when in the real world it did not have the benefit of an interested adversary digging up every possible fact. If plaintiff was unable to show even a scintilla of evidence which could give rise to an inference of antecedent negligence or carelessness in this fact-finding procedure termed a trial, how could it be possibly be required that Foster should have acquired this non-existent knowledge elsewhere.

It would be futile to prolong the discussion by assuming arguendo that Transport Supply did demonstrate specific signs of antecedent negligence or possessed a reputation for carelessness. For the next question that must be raised then is was Foster aware or should Foster have been aware of these. The discussion leads nowhere for without specific examples an analysis cannot be made as to whether under the circumstances Foster should have been aware. It is impossible to discuss what Foster knew, or should have known, when there was nothing for them to know.

**C. THE HARM MUST BE CAUSED FROM THE  
QUALITY IN THE CONTRACTOR WHICH MADE  
IT NEGLIGENT FOR THE EMPLOYER TO  
ENTRUST THE WORK TO HIM.**

The Court's instruction on this issue (R. 163) was based on the Restatement of Torts 2d, Sec. 411. The reporter's comment on the extent of the rule under comment b is as follows:

The employer of a negligently selected contractor is subject to liability under the rule stated in this Section for physical harm caused by his failure to exercise reasonable care to select a competent and careful contractor, but only for such physical harm as is so caused. In order that the employer may be subject to liability it is, therefore, necessary that harm shall result from some quality in the contractor which made it negligent for the employer to entrust the work to him. Thus, if the incompetence of the contractor consists in his lack of skill and experience or of adequate equipment but not in any previous lack of attention or diligence in applying such experience and skill or using such

equipment as he possesses, the employer is subject to liability for any harm caused by the contractor's lack of skill, experience, or equipment, but not for any harm caused solely by the contractor's inattention or negligence.

An application of this rule is found in *Mooney v. Stainless, Inc.*, 338 F.2d 127, cited, *supra*, at page 39. The court stated that there was no evidence that the independent contractor was incompetent and, therefore, the defendant could not be negligent in selecting him. The court went on, however, and stated that they were not at all certain that Stainless would have been liable even if Wood had been shown to be incompetent. They quoted section 411 of the Restatement of Torts and quoted comment b therein. They took cognizance of the fact that in their case plaintiff attempted to prove the independent contractor's incompetence by reason of his alleged lack of equipment and lack of experience. They then took note of the accident and stated that the death of plaintiff's husband seemed to have been caused more by lack of attention or temporary negligence on the part of the independent contractor in operating the truck rather than by lack of experience as a contractor or by any insufficient equipment. Thus, the court concluded that Stainless would not have been liable for this particular accident even if it were shown that the subcontractor had been incompetent since the accident occurred as a result not of his incompetence, but rather temporary lack of attention or negligence.

### **III. THE EVIDENCE FAILED TO ESTABLISH ANY NEGLIGENCE BY FOSTER REGARDING SECTION 322(c) WHICH WAS A PROXIMATE CAUSE OF PLAINTIFF'S INJURY,**

The jury found in answer to a special interrogatory

that Foster was negligent in violating Section 322(c) of the Interstate Commerce Act. (49 U.S.C. Sec. 322(c)). And, that this negligence was a proximate cause of the accident (R. 180). The Court stated the law to be (R. 166):

This law of the United States provides it shall be unlawful for: 'any shipper, or any officer or employee thereof, [to] knowingly except or receive any [rate] concession in violation of any provision of [the Interstate Commerce Act].

At the very least, the statute requires a knowing party, and more probably in addition a willing party, in order to have a violation. Thus there must be substantial evidence, no mere scintilla, of Foster's knowledge of this violation. (See *Ross v. Great Northern RR*, 315 F.2d 51 (9th Cir. 1963). The Court instructed the jury (R. 166) that if Foster knew, or *should have known* that (1) Knight was not authorized by the ICC to perform the interstate shipment and (2) that Transport Supply was charging them less than that which would have been charged by an ICC certified carrier, then they could find that Foster violated § 322(c).

#### **A. THE RECORD SHOWS NO VIOLATION OF THE ACT.**

##### **1. NO SHOWING THAT FOSTER KNEW OR SHOULD HAVE KNOWN THAT KNIGHT HAD NO CERTIFICATE.**

Since it is unquestioned that Knight did not have a certificate there is no question about plaintiff having sustained this portion of his burden of proof. However, the evidence of plaintiff does not show that Foster knew that Knight did not have a certificate

nor does it show that he should have known this.

A review of the record reveals only one occasion when Knight came in contact with Foster. This was at the San Leandro yard of Bigge Drayage when the shipment in question was loaded (360). Knight drove in and announced that he was to take a load of steel rails to Seattle. It was not even shown by the plaintiff that Knight at this point had any contact with Foster. Since Bigge Drayage employees did the loading (474), it was not essential that the Foster watchman or clerk be in constant attendance (475). However, assuming that the employees were in attendance, what was there to put them on notice. They were not instructed to look for markings (485). Even if they were, this would not get them very far for as Mr. Baker testified (674), many carriers have a city truck which picks up from the yards and then returns to the carrier's own yard for staging.

However, the question must come back to what did plaintiff show that would indicate that Foster should have known. He brought in Mr. Edwin Cusick, the manager of Bigge Drayage Trucking Division who testified (454) as to what he would look for on any truck he was renting pursuant to his Interstate Commerce Commission Certificate. But Mr. Cusick was not a seller-shipper whose main purpose is to get the load on the truck as fast as possible and get it on the way to the buyer. Also, Foster did not rent this vehicle — it was loading it. Mr. Cusick's testimony was irrelevant to any issue in the case, and certainly could not qualify as giving any sort of inference into what the reaction of a reasonably prudent shipper would be.

In short, there is no evidence in the record that any reasonably prudent shipper would run out and check each vehicle of each carrier it uses to determine whether its Interstate Commerce Commission numbers are on prominent display or whether, if numbers are displayed, that they are real.

Since the findings required to be made by the jury were stated in the conjunctive (R. 166-7), failure to prove the first by substantial evidence eliminates any necessity to consider the second. Plaintiff herein failed to present anything approaching a substantial amount of evidence by which it could be inferred that a reasonable prudent shipper would make a point of checking a carrier's truck for anything other than proper size. There is not one item of evidence in the record to show that any shipper anywhere at any time felt that this was his duty. The duty of ferreting out uncertified carriers lies with the Interstate Commerce Commission. It is their job and their responsibility to eliminate the violators of the law. This case notwithstanding, they have done their job well. The testimony of Harold R. Gordon, Regional Manager of Foster (488) shows how shippers have come to rely in the past years on the job the Interstate Commerce Commission does. He states that shippers now can simply assume that any carrier who comes in is certified.

However, the overriding consideration remains the same. Foster had a duty not to knowingly break the law. However, it did not have a duty to investigate every truck which pulled into its yards to make sure that the driver was not breaking the law. A duty like this would make every shipper a little arm of the Interstate Commerce Commission. This would

be too onerous a burden for the shipping industry to bear. That there is no duty to inquire is the same conclusion reached by many of the courts who have considered the question involving similar violations of the Interstate Commerce Act and analogous state regulatory acts. See discussion of *Moore, supra* at page 38, *DeBord, infra*, at page 59, *Chickasha, infra*, at page 62, and *Barsh, infra*, at page 64.

In short, the record shows no evidence that Foster knew that Knight was uncertified. In addition, the plaintiff introduced no evidence from which it can be inferred that Foster should have known this. Because of this failure to sustain his burden of proof, plaintiff was not entitled to have this theory of his case go to the jury, and there is no substantial evidence to support the jury's finding.

## **2. NO SHOWING THAT FOSTER KNEW OR SHOULD HAVE KNOWN THAT TRANSPORT SUPPLY WAS CHARGING LESS THAN THE MINIMUM RATE.**

Having failed to sustain by substantial evidence his allegation that Foster should have known that Knight had no certificate, plaintiff was not entitled to proceed on the theory that Foster knew, or should have known, that the amount of charges by Transport Supply to Foster for such shipment were less than that which could be charged by any certified carrier. However, assuming arguendo that plaintiff did provide substantial evidence as to Knight, plaintiff still must be denied recovery since he failed to prove by substantial evidence the second of the conjunctive requirements.

Plaintiff attempted to prove that Foster had actual knowledge of the price by two methods. First, he introduced over objection, evidence of two prior dealings with Transport Supply by Foster through two witnesses (testimony of James Connors (14-23) to which defendants objected (17 and 24), testimony of Jack L. Steward (267) to which defendant objected (269)) and exhibits 6(a) and 6(b). Testimony of both of these witnesses was that Exhibit 6(a) showed that Foster had sent a load out with Transport Supply on November 24, 1963 (19 and 276). They also testified that another load had been sent out by Transport Supply on December 3, 1963 (22 and 279). However, Mr. Steward testified that the invoice by which Transport Supply billed Foster was not even prepared until December 14, 1963, some seven days after the shipment in question was picked up by Knight (278). While plaintiff did not bring out the billing date of the December 3rd shipment, examination of exhibit 6(b) shows that this bill was not prepared by Transport Supply, an Oregon Corporation, much less delivered to Foster's San Francisco office, until December 7th, the morning of which Knight picked up the steel from the San Leandro yard.

Thus, examination of the evidence clearly shows that Foster could have been put on notice by virtue of these two prior dealings because they did not receive any bill from Transport Supply until after Knight had left with the load in question.

The plaintiff also attempted to introduce some material from which he desired the required inference would be drawn by his questioning of the Foster salesman. Here again the effect of the regime of the Interstate Commerce Commission is seen. The sales-

men know from experience it does no good to shop around for a bargain rate. The carriers all charge what the ICC will let them. In addition, they know that the ICC will not let the shippers be gouged. Thus, there is no reason to inquire about price, the main thing, is do you have a big enough truck and how soon can it be here (534 and 549). The situation is reasonable. The Interstate Commerce Commission has done its job well. It has brought economic stability to the shipper-carrier relationship. Competition is now conducted mainly in areas of service, availability and equipment. Price-cutting and discrimination are no longer significant factors which a shipper must consider.

Thus, the record shows that plaintiff failed to establish from the previous transactions that Foster had actual knowledge of Transport Supply's lower rates. In addition, plaintiff did show an ordered economic sector wherin the price to be charged for services, previously the prime overriding consideration, has become substantially subordinated to other considerations.

Plaintiff did not sustain his burden of proof to come forward with substantial evidence that Foster knew or should have known that Transport Supply charged less than the minimum rate. This theory of the case should not have been submitted to the jury.

## B. THE ACT IS INAPPLICABLE IN THIS CASE.

### 1. PLAINTIFFS ARE NOT WITHIN THE GROUP SOUGHT TO BE PROTECTED BY THE STATUTE.

It is generally accepted that the standard of con-

duct required of a reasonable man may be prescribed by legislative enactment. However, it is not every provision of the criminal statute or ordinance which will be adopted by the court in a civil action for negligence. As is stated in Prosser, *Torts*, page 193 (3rd ed. 1964) :

There are statutes which are considered to create no duty of conduct toward the plaintiff and to afford no basis for the creation of such a duty by the court.

This rule is clearly applicable in Washington. The best statement of this rule is found in the case of *Cook v. Seidenberg*, 36 Wash.2d 256, 217 P.2d 799 (1950). Here was a case where a landlord, the defendant, had wilfully refused to provide heat for the tenants as required by a city ordinance. With his knowledge, many of the tenants purchased plug-in electric heaters. One morning, as one of these heaters was being used to supply the heat which the landlord was directed by law to provide, the plaintiff's child's nightgown became ignited and caused serious injury to the child. The court, after a discussion of the question whether the ordinance was aimed at this kind of injury (which will be treated *infra*), stated (page 259) :

We have several times applied the analogous principle set forth in clause (a) of Section 286 Restatement of Torts, to the effect that the violation of a statute, or ordinance is not actionable negligence except with reference to persons intended to be protected by such statute or ordinance.

In the case of *Short v. Hoge*, 58 Wash.2d 50, 360 P.2d 565 (1961), the plaintiff alleged negligence after she fell down the stairway between the 17th and 16th

floors of the Hoge Building in that there was no handrail as required by city ordinance. On page 54 of the opinion, the court set forth the elements plaintiff would have to prove in order to succeed in her action.

In order to establish a *prima facia* case on her theory of negligence *per se*, it was necessary for the appellant to prove (1) the existence of the ordinance, (2) its violation, (3) that such violation was the proximate cause of her injury, and (4) that she was within the class of people that the ordinance sought to protect.

[citing *Cook*, supra].

In the last case to come down from the Washington Supreme Court on this point, *Morgan v. Washington*, [Wash.2d], 71 Wash.D2d 812, 430 P.2d 947 (1967), the court was faced with a wrongful death action against the state. This arose after a two-year-old wandered onto Interstate Highway 5 and was killed. Plaintiffs contended that statute and highway department policy statements required the state to control access to the highway, and their failure to control was the proximate cause of injury. The court stated (page 814):

In any event, it is clear from the language of the statute and the policy statement, that both are intended for the protection of users of the highway, and were not intended to render the state liable to persons who might go onto the highway in violation of the access regulations. Only persons in the class for whose benefit a statute was enacted can claim its benefits.

These three cases show without question that in Washington the rule is that a plaintiff who is basing an allegation of negligence on the violation of a

statute or ordinance must prove that he is an individual whom the statute was intended to protect. Failure to prove that he comes within the protective ambit of the statute results in a collapse of the of the plaintiff's cause of action.

## **2. THE HARM SUFFERED IS NOT THAT WHICH THE ACT WAS INTENDED TO PREVENT.**

In Washington, the rule is that in order to succeed in a negligence action alleging violation of an ordinance as negligence, the plaintiff must prove that the kind of injury involved was that which the ordinance violated was designed to prevent. This requirement was stated in *Cook*, *supra*. Here the court in a lengthy discussion of the requirements of a negligence action based upon an ordinance violation set forth the following:

“The violation of a city ordinance is negligence *per se*. [citing cases] But it is fundamental that such negligence is not actionable unless the statute or ordinance violated was designed to prevent the kind of accident and injury involved in the particular case. [citing cases from Oklahoma, Kentucky, Texas, South Carolina and Prosser]. A statement of this principle, which has been quoted with approval in many cases, is that set forth in 38 Am. Jur., *supra*: ‘It is not enough for a plaintiff to show that the defendant neglected a duty imposed by statute and that he would not have been injured if the duty had been performed. He must go further and show that his injury was caused by his exposure to a hazard from which it was the purpose of the statute to protect him.’ ”

This position was reiterated in the case of *Currie v. Union Oil Co.*, 49 Wash.2d 898, 307 P.2d 1056 (1957).

The question now is, under Washington law, what class of persons were to be protected by the act and what type of risk of harm was the Act designed to prevent. The Interstate Commerce Act has been the subject of extensive litigation ever since its inception in 1887. The act has been many times before the United States Supreme Court, and the supreme courts of the states. There have been many occasions when these courts have passed upon the question of what was the object of the Interstate Commerce Act. One of the earliest interpretations, coming only 5 years after the enactment of the Interstate Commerce Act, is found in the case of *I.C.C. v. Baltimore & O. R.R.*, 145 U.S. 263 (1892). The court, before it turned to the relative merits of the question before it, stated:

“The principle objects of the Interstate Commerce Act were to secure just and reasonable charge for transportation; to prohibit unjust discriminations in the rendition of like services under similar circumstances and conditions; to prevent undue or unreasonable preferences to persons, corporations, or localities; to inhibit greater compensation for a shorter and for a longer distance over the same line; and to abolish combinations for the pooling of freights.”

Casual reading of this statement clearly shows that the thrust of the Interstate Commerce Act was towards economic relations among shippers and carriers. This is borne out by the following cases from the United States Supreme Court: *Louisville & N. RR v. United States*, 282 U.S. 740 (1931). *Midstate Horticultural, Inc. v. Pennsylvania R.R.*, 320 U.S. 356 (1943).

In a later case, *New York v. United States*, 331 U.S. 284 (1947), the Interstate Commerce Commission had

found discriminatory rates in favor of the northeast portion of the United States and ordered a lowering of western rates and an increase in northeastern rates. The court started its opinion thus (page 296) :

“First. The principal evil at which the Interstate Commerce Act was aimed was discrimination in its various manifestations. [citing *Louisville & N. R.R., supra.*] ”

Expression of a similar view, if not the same view, is found in the state court opinions. The case of *New York, N. H. & H. R. R. v. California Fruit Growers Exch.*, 125 Conn. 241, 5 A.2d 353 (1939), is typical. This was an action by the railroad to recover shipping charges. The court, in its discussion of the Interstate Commerce Act, said (page 360) :

“The aim of the Interstate Commerce Act was to secure for each and every shipper of goods in interstate commerce absolute equality of reasonable rates, uniform in application without discrimination or preference.”

The obvious theme running throughout all of these cases is that the Act is intended for a very special purpose. It is aimed at establishing economic stability between shippers and carriers. It is designed to protect shippers and carriers from the disastrous price wars, rate cutting, discriminations and secret rebates which typified the situation prior to the enactment of the Interstate Commerce Act. The harm which the statute was intended to prevent was injury to shippers or carriers by virtue of these practices. There was, of course, a benefit intended to the whole of society. However, this was only an indirect benefit resulting from stability in the shipping industry. The group which was specifically to be protected by this legisla-

tion was the shippers. They were to be no longer at the mercy of the carriers. The activities of the carriers would be watched over from then on. The rates which they set and collected would have to be fair. In addition, the carriers would also benefit to a large extent. They no longer had to fear price wars with other carriers nor be forced to acquiesce to the extortive demands of large shippers. The injury to be prevented by the Act are the kinds of economic injury concomitant with the practices of price wars, rebates, discrimination, and extortion.

The record shows that plaintiffs are neither carrier nor shipper. The injury complained of is personal, not economic. While it might be argued that one of the benefits derived from the regulatory regime of the Interstate Commerce Act is highway safety, this was obviously not the motivating factor behind the Act. Plaintiff can make no claim under the Act since it was passed neither for their benefit personally nor to prevent their type of injury.

#### **C. Violation of the statute was not the proximate cause of plaintiff's injury.**

Assuming arguendo that Foster violated the Act and assuming further that the plaintiffs are within the scope of those who are to be protected and assuming further that their injury is the type of injury which the statute was designed to prevent, the plaintiffs must still be denied recovery because the evidence shows a lack of causal connection between the assumed violation and their injuries. The Washington rule was reiterated again recently in the case of *France vs. Peck.*, ....Wash.2d...., 71 Wash.D.2d 580, 430 P.2d 513 (1967). The court noted that they had

been faced with the question of statutory violations and the consequent harm on a number of occasions (p. 584) :

“The general rule for determining causal connection is set out in *Berry vs. Farmers Exchange*, 156 Wash. 65, 67, 286 Pac. 46, 47 (1930) :

‘That violation of an ordinance, generally speaking, is negligence, there can be no dispute, but the law is well-settled that there must be a causal connection between the negligence arising from the violation of the ordinance and the accident itself before a cause of action arises from such violation.’ ”

The degree of proof which a party must sustain in order to proceed with his cause of action was set forth in the case of *Ward vs. Zeugner*, 64 Wn.2d 570, 392 P.2d 811 (1964). Here the court said (574) :

“Even though plaintiff violated the statute and was thereby guilty of negligence, *per se*, such does not bar plaintiff’s recovery or warrant submitting such violation to the jury, unless there be substantial evidence, as distinguished from a mere scintilla, that the violation proximately contributed to causing the accident.”

This requirement of Washington law that substantial evidence, not a scintilla of evidence, of a party’s negligence and proximate causal relationship between the negligence and plaintiff’s injuries was recognized by this Court in the case of *Ross vs. Great Northern R.R.*, 315 F.2d 51, (9th Cir., 1963). Therein this Court said (page 56) :

“Substantial evidence of appellee’s negligence and the proximate causal relationship between it and appellant’s injuries are required under Washington law. Substantial evidence is required, and

a 'scintilla' of evidence is insufficient under that law."

The particular question of whether a violation of the Interstate Commerce Act, by a shipper's use of an uncertified carrier, can render that shipper liable for negligence on the part of the carrier's employees or contractors has been passed upon several times by both Federal and state courts. The answer to the question has been uniformly that there is no possible causal connection between the use of an uncertified carrier and any injuries resulting from that carrier's negligence. An early case to discuss the question was that of *DeBord vs. Proctor & Gamble Distrib. Co.*, 146 F.2d 54 (5th Cir. 1944). Defendant, Proctor & Gamble, had contracted with White Star Transit Company for the latter to drive one of Proctor & Gamble's trucks from Cincinnati, Ohio, to Rome, Georgia and to there return it to the defendant. The District Judge entered judgment for the defendant. On appeal, plaintiff contended that the lack of an Interstate Commerce Certificate on the part of White Star made the defendant liable. In reply to this contention, the court said (page 57):

"We think it quite plain that the owner had no duty to ascertain whether the motor carrier had complied with the Act, and that the acts of the carrier in performing the contract subjected the owner to no liability, (citing *Marion Machine*, infra at p. 63). But whether so or not is beside the point. The liability here asserted is not one for driving an automobile without a license, but one for damages proximately resulting from the negligence of one for whose action the defendant is responsible. There was no proximate causal connection between driving the car without a license and the injury. The White Star, itself, would not have been liable for injuries caused

while the car was being so driven unless there was actionable negligence proximately causing them (citing cases). For a much stronger reason the defendant would not be, for the evidence showed affirmatively that the truck which plaintiff claims caused his injuries was not in the control of, or being driven by, the defendant or by someone in his employ or under his direction.

"There is nothing mysterious or recondite about the theory on which liability was denied in this case. The burden was on the plaintiff to prove that defendant, or someone for whose action he was responsible, was negligent. He did not prove this. On the contrary, the evidence established that the negligence complained of was not that of the defendant or its servants but of a servant of an independent contractor whom the defendant had employed to do a job for him, reserving no direction or control over the manner or means of doing it. The case, therefore, failed because the element necessary to recover, that the defendant's conduct has been wrongful, has not been proven. The law does not prohibit, it permits, the making of independent contracts. The only thing the defendant did here was to make such a contract. It reserved no control over, it had nothing to do with, its performance. For acts of an employee of the contractor causing damage, it is the contractor and not the owner who must be looked to."

In a more recent case from the Seventh Circuit Court of Appeals, the same result as in *DeBord*, supra, was reached. This was the case of *Kenosha Auto Transp. Corp. vs. Lowe Seed Co.*, 362 F.2d 765 (7th Cir. 1966). In this case the plaintiff contracted to take a caravan of vehicles from Rossford, Ohio, to Baker, Oregon. The vehicles included several wide loads. The accident giving rise to the action occurred when defendant attempted to pass one of the vehicles

on the highway in Illinois. Defendant contended that he should have been allowed to introduce the provisions of the "Illinois Policy On Permits" to show that the plaintiffs were operating in violation of them. The court on appeal concluded that they were properly excluded because the alleged violation was not a proximate cause of the accident. The court remarked (page 769) : "[I]t would be just as logical to reason that the presence of plaintiff's caravan on the highway was the proximate cause as to claim that the violations were." For the proposition that lack of a permit is immaterial unless proximate cause is shown, the court cited *DeBord*, *supra*, and *Hoover*, *infra*.

The case of *Hoover vs. Allen*, 241 F.Supp. 213 (S.D. N.Y. 1965) was an action by stockholders for dissolution of a company and for an accounting. The particular point being considered in the latter part of the opinion (page 257) was whether the failure of the company to register as an investment company in any way affected the alleged waste. The court offered the following analogy to explain why there was no causal connection between the failure to register and the injury alleged.

"We are here dealing with a situation exactly the same as if a cause of action were brought in a federal court under the Interstate Commerce Act containing the following hypothetical allegations: (1) contrary to 49 U.S.C. Section 306(a) (1), defendant operated a common carrier by motor vehicle in interstate commerce upon a public highway without their being in force with respect to such carrier a certificate of public conveyance and necessity issued by the ICC. (2) While so operating in violation of Section 306(a) (1), a motor vehicle owned and operated by defendant was negligently driven through a red

light, hitting and injuring plaintiff.

"Obviously, in the suppositious case, there is no causal connection between the lack of a certificate of public conveyance and necessity and defendant's negligently driving through a red light. *Newsome vs. Dunn*, 103 Ga. App. 656, 120 S.E. 2d 205 (1961); see *DeBord vs. Proctor and Gamble Distributing Company*, 146 Fed. 2d 54, 57 (5th Cir. 1944).

"By a parody of reason, there is in the case at bar, no causal connection between the mere failure to register and the alleged acts of corporate waste."

Prosser analyzes the situation this way.

"When a car is driven without a license, the act of driving the car certainly causes a collision; the absence of the license, or the existence of the statute, of course, does not. What the statute does, or does not do, is to condition the legality of the act, and to qualify or characterize it as negligent. Upon cause and effect it has no bearing at all." Prosser, *Torts*, page 195 (3rd Ed. 1964).

The conclusion reached by the Federal courts as to the lack of causality between failure to have a license or a certificate and subsequent injury has also been reached by state courts. One of the early cases was *Bradley vs. Chickasha Cotton Oil Company*, 184 Okla. 51, 84 P.2d 629 (1938). In this case the plaintiff had been struck by a truck being driven by one Mr. Walters. This driver was the employee of a Mr. Moore, the owner of the truck. The trial court dismissed Chickasha, the shipper, as a defendant and plaintiff appealed this. The facts reveal that Chickasha had a contract with Moore calling for Mr. Moore to deliver defendant's cotton oil. The court in its discussion

pointed out that Moore was a class B motor carrier, but had no class B permit. Rather, he was operating under Chickasha's Class C permit. For the purpose of discussion, the court assumed this procedure to be invalid. Thus, the situation with which the court was working was one wherein a shipper knowingly allowed an uncertified carrier to haul its goods. The court said (84 P.2d at p. 632) :

"With respect to this phase of the question, the legal situation is similar to instances where one loans his license plates to another, or loans his auto to an unregistered or unlicensed person without knowledge of carelessness of the driver. In such instances, although the owner is usually violating the law, just as the driver himself is violating the law, he is not held to civil liability for injury to third persons unless the violation and the injury had causal connection."

The court then cited cases from many jurisdictions for this rule and concluded that there is no causal connection between a shipper shipping on an uncertified carrier and a subsequent accident. This principle was shortly thereafter reaffirmed in the case of *Marion Machine, Foundry & Supply vs. Duncan*, 187 Okla. 160, 101 P.2d 813 (1940). The defendant (Marion Machine had contracted with a private carrier for the latter to haul oil tubing belonging to the defendant from Texas to Oklahoma. While the truck was being operated by the carrier's employees, the accident occurred. There was evidence that the carrier did not obtain a permit for this trip. The Court pointed out the rule that the failure of the carrier to have a permit would not give rise to negligence on the part of the shipper unless there was a causal connection between failing to obtain the permit and the accident. The court could find none. After a discussion of the general liabilities of a

principal for engaging an independent contractor, the court stated (101 P.2d at 816):

“Ordinary hauling by truck is neither inherently dangerous nor unlawful. The shipper is under no duty in this state to ascertain whether the motor carrier has complied with the motor vehicle laws or to inquire into the nature and adequacy of his equipment.”

The case of *Barsh vs. Mullins*, 338 P.2d 845 (Okla. 1959) is very similar to the case under consideration. Here the plaintiff was suing the shipper of goods and the carrier. The plaintiff alleged a conspiracy among the shipper, the carrier and a second carrier to illegally make use of the former carrier's Interstate Commerce Certificate. One of the problems plaintiff ran into, however, was that of releases. For this reason, he had to prove independent negligence on the part of Kerr, the shipper. One of the allegations of independent negligence charged against the shipper was that it permitted the second carrier to haul its shipment in interstate commerce knowing that this second carrier did not have an ICC permit. The court stated (page 851):

“If this was negligence per se considered independently of the conspiracy, for the reason that it constituted Kerr an aider and abetter in violation of Federal statutes governing shipments in interstate commerce, such negligence alone had no causal connection with the accident. [citing *Chickasha*, supra.] Plaintiff argues that there was causal connection in that if Barsh Produce Company [the second carrier] had been licensed by the Interstate Commerce Commission, they could not have employed an unqualified driver. This does not follow. It is true that Hall was not a qualified driver according to the Interstate Commerce Commission's safety regulations but even if

Barsh Produce Company [the second carrier] had been licensed, they could have, nevertheless, employed an unqualified driver if they so desired."

Plaintiff also made a contention that Kerr, the shipper, was guilty of independent negligence in that they failed to check the qualifications of the driver. In the syllabus by the court, it rejects this contention out of hand.

"A shipper is under no duty to inquire into the qualifications of an independent motor carrier's driver."

Thus keeping in mind the Washington rule that there must be substantial evidence of the causal connection between the injury complained of, and the alleged negligence, the record shows that plaintiff failed to bring forth sufficient evidence to make this a jury question. In fact, the record shows that this was not a question for the jury, for there could be no possible causal connection between the assumed violation of the statute and the harm sustained. The record shows that the injury came as a result of brake failure, and this failure was in turn caused by the failure of the driver to either check his brakes or to properly adjust them during the trip. In any event, it is clear that the accident occurred not because Foster entrusted his goods to an uncertified carrier, but because the driver of the truck failed to check his brakes. It is only by engaging in the sheerest form of speculation that it can be said that if the carrier were certified, then the driver would have checked his brakes. This is meaningless guessing. The proximate cause of the accident was Knight's negligence. This was the only cause of the accident. Whether or not Foster knowingly gave his goods to an uncertified driver or

whether or not Foster knowingly shipped for below the minimum rate are irrelevant considerations on the issue of what was the proximate cause of the accident.

As noted above, the courts have uniformly held that there can be no causal connection between a shipper entrusting his goods to an uncertified carrier, and any subsequent injury resulting from negligence on the part of the carrier's independent contractors or employees. There was no legal basis for the trial court to submit this issue to the jury, and the court erred in so doing.

#### **IV. THE RIGHT TO A NEW TRIAL BECAUSE OF SPECIFIC PREJUDICIAL RULINGS.**

Appellant's position is that the lower court should have entered judgment for the reasons heretofore stated, and that it also, under Rule 50, should have granted a new trial. If this Court is of the view that the reasons already given did not warrant a directed verdict, those reasons as well as the additional reasons treated in this part of the brief should be considered in determining whether there should not be a new trial. As was stated in *Aetna Casualty & Surety Company vs. Yeatts*, 122 F.2d 350, 352-3 (4th Cir. 1941) :

“On such a motion it is the duty of the Judge to set aside the verdict and grant a new trial, if he is of the opinion that the verdict is against the clear weight of the evidence . . . or will result in a miscarriage of justice, even though there may be substantial evidence which would prevent the direction of a verdict.”

Of course, in a long trial where many rulings are made, the mere existence of error is insufficient to reverse a lower court for refusing to grant a new

trial. Where, however, as is believed to be true in this case, there is fundamental and prejudicial error in a single ruling or in an aggregation of rulings, reversal is appropriate. Each one of the points treated herein, therefore, is presented not only for its individual merit but also for its overall significance.

#### **A. THE CHARGE AS TO WHAT WOULD CONSTITUTE VIOLATION OF THE ACT WAS REVERSABLE ERROR.**

The Court's instruction on Sec. 322 (c) was erroneous. The Court's instruction said (892) (R. 616):

"The third ground of recovery asserted by plaintiffs against the defendant Foster Company is based on a violation of the Federal Interstate Commerce Act. This law of the United States provides it shall be unlawful for:

“‘Any shipper, or any officer or employee thereof [to] knowingly accept or receive any [rate] concession in violation of any provision of the [Interstate Commerce Act.]’

“For convenience, this section of the law will be referred to as ‘Section 322.’”

and then the Court said (893):

“If you find it has been established by a fair preponderance of the evidence that employees of Foster Company at or prior to the time the cargo of steel in question was loaded at San Leandro, California for interstate shipment to the State of Washington knew, *or in the exercise of reasonable care should have known*:

“1. That the defendant Knight did not hold a valid certificate or permit issued by the Interstate Commerce Commission authorizing Knight or his vehicle to perform interstate transportation of the shipment, and

"2. That the amount of charges by Transport Supply Company to Foster Company for such interstate transportation was less than the minimum rate Foster Company would have been required to pay for such transportation by a carrier, which was certified by the Interstate Commerce Commission, then you may find that Foster Company, as a shipper, violated the above stated provision of Federal Law, Section 322, and such violation, if you find it occurred, would constitute negligence as a matter of law." (Italics added)

Thus, the Court said the jury could find that a statute, which required *actual* knowledge for its violation, had been violated even without the requisite actual knowledge. This does not make good sense and it is not the law.

The statute clearly requires by the plain meaning of its words a knowing violation. In a criminal case this knowledge must be proved beyond a reasonable doubt. In a civil case the plaintiff must at least prove knowledge by a preponderance. However, the charge to the jury did not require that the plaintiff prove actual knowledge by a preponderance. It only required him to prove that Foster should have known. This is not sufficient to show violation.

The question of what constitutes knowing violation of the Act has been treated by several courts. In the case of *Inland Freight Lines vs. United States*, 191 F.2d 313 (10th Cir. 1951) the court had on appeal a conviction for knowingly keeping false drivers' logs as a part of its records. In referring to the trial court's instruction, the court said (316):

"The primary substance of the instruction was that *mere negligence* on the part of the company

in accepting the false logs without investigating as to their falsity was sufficient to warrant a conviction." (Italics added)

The Court held the instruction to be prejudicial error and reversed and remanded.

In a more recent case, *United States vs. Joralemon Bros., Inc.*, 174 F.Supp. 262 (E.D.N.Y. 1959), the Court was faced with an alleged violation of the act on the part of a motor carrier. The Court said mere occurrences of violations would not constitute criminal acts. "A knowing and willful act, within the meaning of the aforesaid statute, is one that is conscious and intentional, deliberate and voluntary, rather than merely negligent." (P. 263).

Thus, it is clear that the statute is not like most criminal statutes used to form a basis for civil liability growing out of an automobile accident, as for example, speed limit law, rules of the road, and equipment statutes. It requires a knowing violation. Nothing less will sustain a finding of violation. No mere negligence is sufficient. Under the charge, if the jury felt Foster should have known it was violating the act, then they could find it knew it was violating the act. This error undermines the whole consideration of the jury and is sufficiently prejudicial to warrant a new trial.

#### **B. ADMISSION OF TESTIMONY REGARDING THE REPUTATION OF THE CLASS OF UNCERTIFIED CARRIERS.**

Since plaintiff was unable to produce one witness, or one piece of evidence concerning the antecedent reputation of Transport Supply, he attempted to dis-

charge this burden by the witness, Mr. Landsburg (640). He testified that in his experience with the ICC, he had become aware of a problem with the class of uncertified carriers (643). He also testified that it was common knowledge among "people in the shipping industry, for instance, certainly in the regulatory industry" (647) that uncertified carriers did in fact operate. He then went on to give a long statement concerning how some shippers would get together with some uncertified carriers and cut rates. He concluded with the statement that these "people ultimately go broke and they leave sometimes bloody accidents . . ." (650). He also testified that ICC road checks reveal that in the majority of cases uncertified carriers' equipment was in bad condition (651).

To all of this testimony the defendants strenuously objected urging "proof of what some other group of people do is no proof of what another does at a specific time or place" (643), and "any law enforcement agency has problems, and that doesn't mean that some specific individual [whereupon the court cut him off, 644]" and "he [plaintiff] is going to try to prove a reputation of one person by the reputation of a class, which is not proper" (645).

In a tort action, the trier of the fact is to be concerned only with what certain people did on certain occasions under certain circumstances. Testimony as to what other people did on other occasions under unknown circumstances has no bearing on the issues involved, and is therefore irrelevant, and hence, inadmissible. The witness's entire testimony was taken up with what he had observed other people do at other times. The witness did not once refer to the defendant Transport Supply or to the defendant Knight or to

the defendant Foster. Rather he stated that sometimes uncertified carriers and shippers get together and leave "bloody accidents" on the highway. This, it is submitted, was absolutely irrelevant to any issue in the case. But more than that it was disastrously prejudicial to Foster. This witness's irrelevant testimony left the clear impression that Foster and Transport Supply had gotten together for an illegal deal in which they cared not how many bloody bodies were strewn along the roadside. The thrust of this witness's testimony was to tell the jury here is your chance to help clean up the highways by laying liability to the shipper.

The general rule is that evidence of the reputation of an individual for negligence is inadmissible. See *United States vs. Compania Cubana DeAviacion*, 224 F.2d 811, 820 (1955); 29 Am.Jur.2d, *Evidence* Section 316; McCormick, *Evidence* Section 155 (1954); 5 Wash. Prac. Section 3 (1965). An exception allows in evidence of an *individual's* reputation when that *individual's* reputation is in issue. See 5 Wash. Prac. Sec. 2 (1965); 29 Am.Jur.2d, *Evidence* Sec. 337; McCormick, *Evidence* Sec. 154 (1954). However, nowhere is it ever hinted that a party may prove the reputation of an individual by proof of the reputation of a class of which he is a member. In fact it follows a fortiori from the rules stated above that this kind of testimony is always inadmissible.

The plaintiff claimed that the evidence was admitted only to show what Foster should have known (645). How this witness would know what a shipper would know, or should know, was not shown except by the bootstrap technique of the witness himself. Moreover, the court did not instruct the jury that this witness

was testifying only as to what Foster should know. The net effect of the testimony was to tell the jury that here is your chance to help the ICC in a problem whether or not this particular defendant was negligent. The admission of the testimony of this one witness threw the whole fact finding procedure out of alignment, and this is grounds for a new trial.

### C. THE REPETITIVE ADMISSION OF EVIDENCE AS TO UNLAWFUL RATES WAS ERROR.

Since plaintiff had no substantial evidence to support his theories, he had to rely on the techniques of confusion and prejudice. He used the prejudice mainly with Mr. Landsburg. With the witnesses Connor and Stewart he pursued the course of confusion. Plaintiff's efforts with these two witnesses were largely centered in attempting to convince the jury that Foster was on trial for shipping at an illegal rate. He went through each of the four invoices sent by Transport Supply to Foster, and inquired as to each whether this was a lawful rate. Each of the two witnesses dutifully replied that this was not a legal rate (20, 23, 27, 31, 277, 280, 285, 287, 288, 289). All of this, despite the fact that only two of the invoices were for shipments before the one in question, and that none of them were in fact even received by Foster prior to the shipment in question.

By the time plaintiff stopped hammering in the fact that Transport Supply did not charge the legal minimum, the jury was well-convinced that this was more of a criminal case than a civil case and that they should convict Foster of something somehow. The latter two exhibits to which these witnesses were referred (6(c) and 6(d)) were absolutely irrelevant to

any issue in the case since they were not prepared until after the accident in question. In addition, all of the exhibits (6(a), 6(b), 6(c) and 6(d)) were inadmissible since none arrived prior to the shipment in question, and the charges reflected therein could not possibly be a proximate cause of the accident.

The court's allowing of plaintiff to confuse and mislead the jury in this manner was reversable error.

**D. THE ADMISSION OF EVIDENCE AS TO WHAT  
A CARRIER WOULD LOOK FOR WAS  
ERRONEOUS.**

The witness Cusick testified as to what he as an ICC certified carrier would look for on a new truck he was leasing (454). The defendant moved to strike all of his testimony as irrelevant (456). The court instead of granting this motion told the jury they could use the testimony in any way they wanted (457).

The admission of this testimony in the first place was clearly erroneous. The testimony of what a certified carrier would look for is irrelevant to the issue of what a shipper should look for. Most important, neither Foster, nor anyone else involved in this litigation, leased or rented any trucks or equipment of any kind whatsoever. Moreover, to compound the error and add to the confusion of issues which the plaintiff was pursuing, the court's ruling was error of such magnitude that, if for no other reason, justice demands that Foster have a new trial.

**E. THE CHARGE ON THE APPLICABILITY OF SAFETY STATUTES AND REGULATIONS WAS REVERSABLE ERROR.**

After the plaintiff had prejudiced the jury through Landsburg's "bloody accidents" and confused them through Connor's and Stewart's illegal rates, the court then magnificently compounded the whole mass of prejudice and confusion by instructing them that the safety statutes and regulations, which by their very language apply only to motor carriers, could be applied to the shipper (833, R. 157-159, App. Br. p. 28).

This one instruction alone threw the whole consideration of the case by the jury into areas where they should not have been allowed to go. It introduced irrelevant considerations to the determination of Foster's liability and allowed the jury to speculate wildly.

**F. THE CHARGE AS TO PROXIMATE CAUSE WAS REVERSABLE ERROR.**

The Court's charge to the jury on proximate cause (875-76 R. 153) was an erroneous statement of the Washington rule on proximate cause. The Court began with the instruction recommended by the Washington Supreme Court Committee on Jury Instructions, 6 Wash. Prac. Sec. 15.01 (1967). This is a one-sentence instruction which succinctly and clearly states the rule. However, the Court did not stop there. It went on and instructed that any act which it found was a necessary antecedent to the injury is negligence, using the following language:

If a particular negligent act or omission in-

itiates a series or chain of causation, in which each connecting causative factor is proximately caused by the preceding factor and in turn proximately causes a succeeding factor, and the unbroken sequence finally causes injury or damage, such end result, in law, is chargeable to the negligence which initiated the series or chain of causation.

This is the "but for" test of proximate cause. It is not the law in Washington.

A recent case to discuss the question of proximate cause was *Mehrer vs. Easterling*, ..... Wash. 2d ....., 71 Wash. D.2d 102, 426 P.2d 843 (1967). In the course of its discussion of legal causation, the Court quoted from an earlier opinion (Wash. D.2d at page 105) :

There is, of course, a distinction between an actual cause, or cause in fact, and a proximate, or legal, cause.

An actual cause, or cause in fact, exists when the act of the defendant is a necessary antecedent of the consequences for which recovery is sought, that is, when the injury would not have resulted 'but for' the act in question. But a cause in fact, although it is a *sine qua non* of legal liability, does not of itself support an action for negligence. Considerations of justice and public policy require that a certain degree of proximity exist between the act done or omitted and the harm sustained, before legal liability may be predicated upon the 'cause' in question. It is only when this necessary degree of proximity is present that the cause in fact becomes a legal, or proximate, cause.

Thus it is clear that the trial Court erred in giving a "but for" instruction on proximate cause. Since this instruction permeated every consideration by the

jury, the error constitutes reversible error.

## CONCLUSION

Plaintiffs did not voluntarily choose to become involved in this lawsuit. However, once they did, they looked around at everyone who had even the remotest connection with the incident giving rise to the suit. In an accident resulting from a driver's inattention to his brakes they attempted to hold liable not only the driver and the owner of the truck, but also the carrier which had contracted with the trucker. In addition, plaintiffs reached back and attempted to place liability on the dealer who sold the truck. Finally, they attempted to lay responsibility, and hence liability, to the shipper which had sold the goods being transported to buyer.

There being no theory in law by which a principal is liable for the negligent acts of independent contractor's sub-independent contractor, the plaintiff pursued two other theories: (1) the selection of an incompetent independent contractor, and (2) violation of a statute. However it developed that plaintiff lacked an essential step in his first theory. There was no evidence of any antecedent negligence by the independent contractor. On his second theory, plaintiff was faced with the problem that he could not prove a knowing violation, could not show he was within the group of persons to be benefitted by the statute, nor even show that an assumed violation was a proximate cause of the accident. Thus, plaintiff proceeded with prejudice and confusion. He introduced testimony about the "bloody accidents" of uncertified carriers. He hit again and again on lawful rates until the jury thought they were trying a criminal

case. This was then compounded by the Court's defective instructions, particularly the charge which applied the motor carrier's statutes and regulations to the shipper and the faulty instruction on proximate cause.

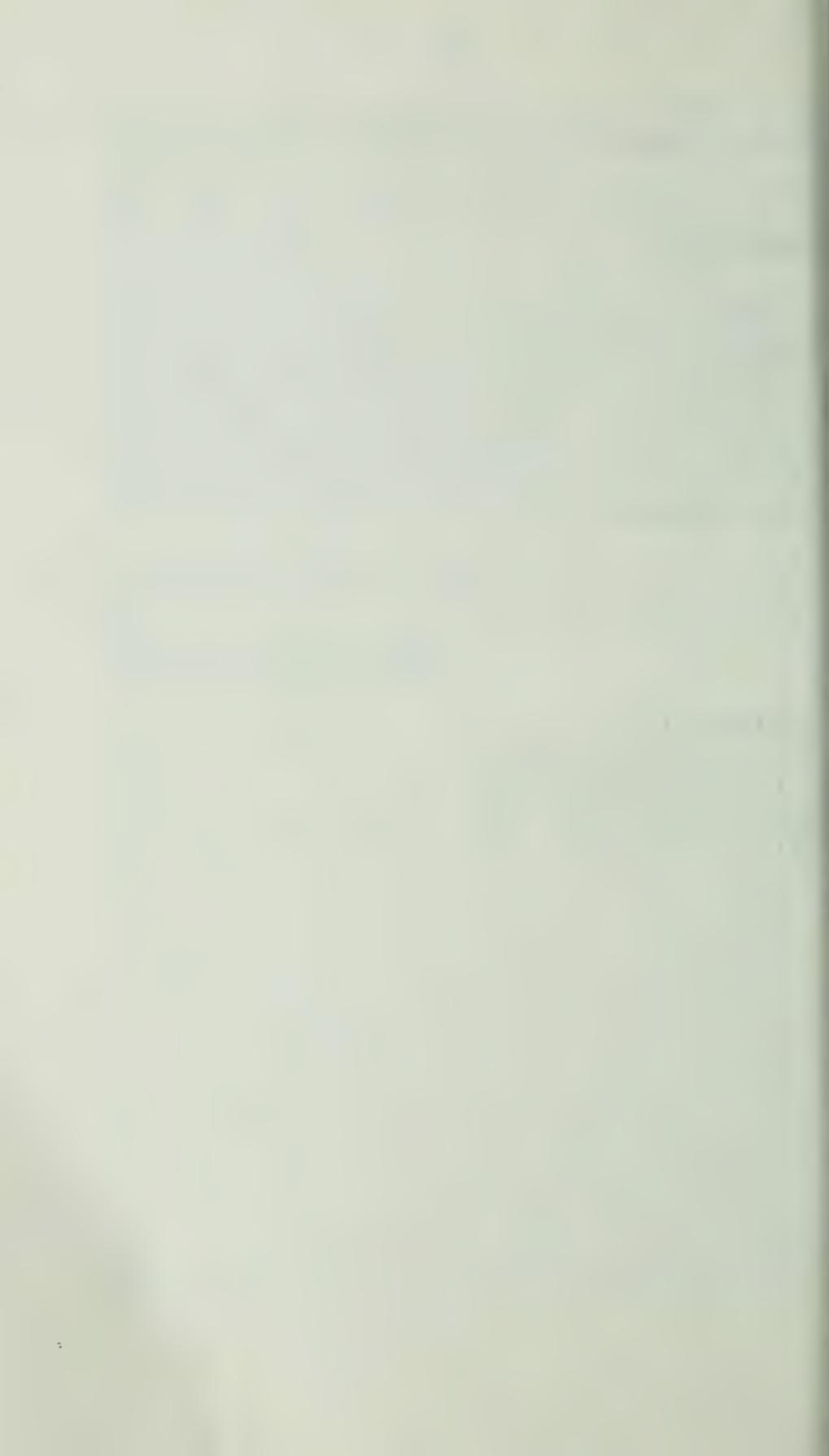
The facts of this case and all fair inferences to be drawn do not establish any negligence on the part of appellants. To permit the verdict to stand notwithstanding the many prejudicial errors would cause an unjust result in this case. The judgment of the Court below should be reversed, and the appellants dismissed as defendants therein.

Respectfully submitted,

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## **Appendices**



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2A-F, Incl.	87
3A, B, C	193
4	667
5A, 5B	24
6	No reference in transcript
7	No reference in transcript
8	No reference in transcript
9	Not admitted
10	Not admitted
11	Not admitted
12A	Not admitted
12B	20
12C	20
13	For Court
14	Not admitted
15	162
16	For Court
17	667
18	No reference in transcript
19A	739
19B	740
19C	742
19D	742
19E	743
19F	743
19G	713
19H	715
20	Not admitted
21	For Court
22	761
23	173
24	177
25A & 25 B	578

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\* Almost all exhibits were identified prior to trial. They were to be admitted without further proof if otherwise admissible by being admitted that each was what it purported to be (R. 132). The page reference is to the transcript of the testimony where the exhibit was admitted in evidence.



## **CERTIFICATE OF COUNSEL**

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion the foregoing brief is in full compliance with those rules.

---

*Attorney for Appellants*



In the  
**UNITED STATES  
COURT OF APPEALS  
FOR THE NINTH CIRCUIT**

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L. B. FOSTER COMPANY, INC., *Appellant*,

vs.

MELVIN HURNBLAD and GRACE HURNBLAD, his wife,  
*Appellees.*

SIM KNIGHT; L. B. McGOWAN; TRANSPORT SUPPLY  
Co., a corporation; NELSON IRON WORKS, INC., a cor-  
poration; and DAVID PAUL'S EASTPORT DODGE, INC.,  
*Defendants.*

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APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION

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**APPELLEES' ANSWERING BRIEF**

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COMFORT, DOLACK, HANSLER & BILLETT,  
*Attorneys for Appellees,*  
Tacoma, Washington 98405

JUL 12 1968



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No. 22597

In the

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L. B. FOSTER COMPANY, INC., *Appellant*,  
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MELVIN HURNBLAD and GRACE HURNBLAD, his wife,  
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SIM KNIGHT; L. B. McGOWAN; TRANSPORT SUPPLY  
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APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION

---

**APPELLEES' ANSWERING BRIEF**

---

**STATEMENT OF PLEADINGS AND  
JURISDICTIONAL FACTS**

Appellees, Melvin R. Hurnblad and Grace M. Hurn-  
blad, are husband and wife and were injured in a  
truck-auto collision that occurred on December 9,  
1963, at Tacoma, Washington. The appellees filed this  
action in the Superior Court for Pierce County,  
Washington, where they reside, alleging liability in

excess of \$10,000 on the part of defendants Sim Knight, L. B. McGowan and Transport Supply Company, all residents of Oregon, and Nelson Iron Works, Inc., a Washington corporation, for negligent acts and omissions. Thereafter by appellees' amended complaint appellant L. B. Foster Company, Inc., a Pennsylvania corporation, and additional defendant David Paul's Eastport Dodge, Inc., another Oregon resident, were named parties on the basis of alleged negligence. When appellees nonsuited defendant Nelson Iron Works, Inc., the only defendant residing in Washington, appellant and other defendants caused the removal of the case to the District Court for the Western District of Washington, Southern Division, under 28 U.S.C.A., §§ 1441-1446, that court having jurisdiction by virtue of 28 U.S.C.A., § 1332. (R. 1-30.)

Defendant Transport Supply Co. failed to answer and was defaulted (R. 186-187). Defendants Sim Knight, L. B. McGowan and David Paul's Eastport Dodge and appellant answered and denied negligence (R. 1-35). Upon trial to a jury, a \$75,000 verdict was returned for appellees against defendants Sim Knight, L. B. McGowan and appellant. (R. 176-177.) After the entry of judgment and the denial of its new trial motion, appellant gave notice of appeal herein (R. 181-190). Defendants Sim Knight and L. B. McGowan did not appeal. Jurisdiction of the appeal is vested in this court by 28 U.S.C.A., § 1291.

## STATEMENT OF THE CASE

### 1. Introduction

. . . A fair statement of the evidence is all that is required for the record on appeal, but the appellant should use good faith to make such statement a full and fair one, so that the burden is not cast upon the court or appellees to make a new one.<sup>1</sup>

Appellees can not accept or admit appellant's statement as full, fair or correct. A new statement of the case is compelled.

### 2. Stipulated Facts

Agreed facts set forth in the pretrial order show appellees are Pierce County residents who were proceeding in their 1961 Ford station wagon in an easterly direction on South 25th Street, Tacoma, on December 9, 1963. Appellee Melvin R. Hurnblad was driving and his wife was sitting in the right front passenger seat. At approximately 8:05 in the morning appellees' automobile entered the Pacific Avenue intersection, which is controlled by a standard overhead red and green traffic signal. Midway through the intersection appellees were seriously injured when their automobile was struck on the right side by a 1945 Peterbilt tractor, pulling a 1945 Pointer Willamette trailer and headed north on Pacific Avenue. The combined truck was 40 feet in length. It was driven by defendant Sim Knight, a co-purchaser with defendant L. B. McGowan. They bought the truck on contract

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<sup>1</sup> *Phillips v. The Governor & Co.* (C.A. 9), 79 F. 2d 971, 975 (1935); 27 USPQ 229.

from defendant David Paul's Eastport Dodge, Inc., a predecessor in interest of Dodge City, Inc. (R. 112-135.)

At the time of the accident the truck was carrying a load of appellant's steel from San Leandro, California, to Seattle, Washington.<sup>2</sup> Appellant placed the shipment order with defendant Transport Supply Company. Appellant agrees the hauling rate it paid was but \$0.75 per hundredweight. (R. 112-114.)

### **3. Proved Facts**

Appellant would have this court believe

. . . there was no evidence concerning whether Transport Supply had the necessary (Interstate Commerce Commission) licenses and permits. (App. Br. 38.)

Exhibit 12D is an Interstate Commerce Commission<sup>3</sup> certification that defendants Sim Knight, L. B. McGowan and Transport Supply Company have never been licensed or authorized to engage as a common carrier in interstate commerce. Exhibit 12D was admitted into evidence when appellant indicated no objection except as to relevancy. (Tr. 940-941.) In addition to Exhibit 12D, there is testimony from which this court can only conclude that defendants Sim Knight, L. B. McGowan and Transport Supply Company had no federal authority when appellees were injured (Tr. 429-430). Nor did any defendant have authority to transport appellant's steel intrastate (Exs. 12B & 12C; Tr. 341-342, 429-430).

<sup>2</sup> The load consisted of 35,000 pounds of rails and 562 pounds of splice bars (Ex. 5A).

<sup>3</sup> Hereafter called the I.C.C.

As previously indicated, the parties stipulated appellant contracted to ship its steel from California to Washington via defendant Transport Supply Company, an unlicensed carrier, for \$0.75 per hundred-weight (R. 112-115). This rate was unlawful, far below the lawful charge of any legitimate interstate carrier (Tr. 23-27, 272-286). Felix Baker, appellant's salesman who arranged the deal with defendant Transport Supply Company, admitted knowing the lawful rate was at least \$1.00 per hundredweight (Tr. 509, 536-537).<sup>4</sup> The major significance of appellees' proof that appellant shipped its steel with an illegal carrier at a cut-rate price is found in the testimony of Frank E. Landsburg, who for 27 years was an employee of the I.C.C. He retired in 1962 as I.C.C. regional manager and district director for the states of Idaho, Washington and Oregon, and now continues as a trucking consultant and safety and traffic expert (Tr. 640-641). Mr. Landsburg testified:

Q. (Mr. Hulscher): Now, the question is, sir, what was the common knowledge among these people (shippers) concerning unregulated and uncertified carriers?

A. Well, generally speaking, people in the shipping industry, for instance, certainly those in the regulatory industry, knew these people were operating illegally on the highway, and they knew too that if they risk becoming a party to a con-

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<sup>4</sup> He also admitted general knowledge as to the existence of unlawful carriers:

THE COURT: You were aware that there were such (unlicensed, unregulated carriers) in 1963 when you made this transaction?

THE WITNESS: I would say yes, that I was aware there were people of that type. (Tr. 536.)

spiracy to violate the law or they aided or abetted these people in their violation, they would be liable to criminal prosecution in the federal courts, they knew that, common knowledge.

Q. What common knowledge did they have of the activities of the unregulated and uncertified carriers operating in interstate commerce?

A. Well, I would say they had complete knowledge. (Tr. 646-647.)

.....

THE COURT: What relation, if any does this (rate concession by unauthorized carriers) have to safety on the highway?

THE WITNESS: Very well, now, lets take the unlawful operator.

(Mr. Hulscher) Alright. Go ahead.

A. In order to make a deal with the shipper and prevail upon the shipper to risk the possibility of being a party to the criminal action in the courts, this unlawful operator had to make a substantial reduction in the published rates of the common carriers in order to get the shipper to take that risk. Therefore, he did not have the money, because of his drastically reduced income, to properly maintain his truck in a safe operating condition. He found it necessary to violate practically every pertinent section of this Interstate Commerce Act in order to stay on the highway. (Tr. 648-649.)

Of importance, too, is the testimony of Jack L. Stewart of the Willamette Traffic Bureau, an agency which represents legitimate, irregular route motor carriers before the I.C.C. and publishes their rates. Willamette Traffic Bureau has a file on every known carrier on the Pacific Coast. (Tr. 267-268.) Mr. Stewart stated

there are persons active in the illegal transportation of goods, known as gray area operators, who charge less than lawful rates. These unlawful carriers are not in business any length of time. Their rates are so low they have no money to spend on proper maintenance and renewal of equipment. Even if they start operating with safe equipment, it soon becomes dangerous. The problem exists throughout the United States. (Tr. 274-275.)

Returning to the testimony of Mr. Landsburg, he elaborated further:

(By Mr. Hulscher) May I interrupt for just a moment. These things that you have just referred to, were these things common knowledge among shippers, carriers, and regulatory agencies that were involved in interstate commerce in 1963?

A. It is well known because these people ultimately go broke and they leave sometimes bloody accidents and unpaid bills, and it was an economic loss, and it was known by everybody.

Q. This is again known in 1963?

A. Oh, yes.

Q. Now, was there any general knowledge — maybe you have answered this, but I will ask it to see, was there general knowledge in the industry among shippers, carriers, and regulatory agencies concerning the maintenance on equipment operated by non-certified and/or unregulated carriers in interstate commerce in 1963?

A. Yes, sir, it was common knowledge.

Q. What was that?

A. Borne out by our road checks.

Q. What was that knowledge, sir?

A. Well, that knowledge was that their equipment was usually in very bad condition, and in the majority of cases, it was unsafe for operation on the highway.

Q. From your experience in this field, do you know why the equipment of the uncertified and unregulated carrier was generally run down?

A. They didn't have the money to pay the repair bills. They had cut the rates drastically, the income was below their costs, most of them were usually ignorant people, and they didn't have any business idea what their costs actually were. (Tr. 650-651.)

It is clear appellant employed an unauthorized carrier at a cut-rate to carry appellant's mine rails to the state of Washington (Exs. 5A, 5B, 12B; R. 112-115; Tr. 20-32, 267-290). And what is in the record about the quality of the trucking equipment of appellant's unlicensed carrier? The tractor-trailer rig was more than 18 years of age (R. 114). It appeared to be old and rundown (Tr. 111, 209-214, 700). A trucker witness described the tag axle as among the oldest he has ever seen (Tr. 225). The paint job evidenced a large splice in the midsection of the trailer (Tr. 111-112). Neither the tractor nor trailer bore an I.C.C. number or other indicia of its approval or sanction (Tr. 266). A witness said the truck appeared suitable only for hauling a light cargo of hay, perhaps to 25,000 pounds (Tr. 714). Another driver said Pacific Intermountain Express, a valid common carrier, would never make use of equipment alike that which carried appellant's steel rails on the trip to Seattle;

nor would such usage be permitted by the I.C.C. (Tr. 113).

Appellant's carrier's truck lived up to its appearance. Appellees proved it really was in poor mechanical condition. Witnesses testified it was unsafe to drive (Tr. 117, 200, 587, 777). At the accident scene the brakes were so badly worn and out of adjustment a pencil was easily inserted between the linings and drums with the brakes applied (Tr. 105-107, 684-685, 707-708). Later on a closer, detailed inspection revealed one brake on the tractor's drive axle had little braking power. The wear on the lining was into its rivets (Tr. 169). This claim is substantiated by Exhibit 23, a brake shoe brought to court (Tr. 181-183).

Mr. Gene McCoy, who salvaged the truck, said the brake shoes on both wheels of the tractor's tag axle were worse than Exhibit 23, and the brakes were far out of adjustment (Tr. 187-190).<sup>5</sup> Even proper adjustment, in his opinion, would have been futile because the brakes were too far gone (Tr. 188, 190, 200). Mr. McCoy also examined the forward axle of the trailer. He found one wheel had no brake lining, indicating it had no braking power whatsoever (Exs. 3A & 3B; Tr. 191-192). The other wheel was down to half of its brake lining (Tr. 191-192). As far as concerns the wheels on the rear trailer, Mr. McCoy found their linings were completely shot (Tr. 198-200).

Both brake drums on the tractor's tag axle were

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<sup>5</sup> A witness called by the defense, Mr. James Rogers of the Washington Public Service Commission, corroborated the view the truck's brakes were out of adjustment. (Tr. 708).

oversized, as were the drums on the rear axle of the trailer (Tr. 198-199). The significance of said defects is that the truck's brakes were satisfactory for light hay loads only, but not for heavier loads (Tr. 209, 239). One witness testified in effect it was a minor miracle the truck reached as far as Tacoma on its journey from California before having the accident (Tr. 138-139). All in all, the jury was justified in concluding the truck was unsafe in appearance and in actuality when utilized by appellant to carry its steel. (Tr. 133, 156, 164-214.)

There is also evidence in the record bearing on the incompetency of defendant Sim Knight, the truck driver. Witnesses said he should have known of the poor condition of his brakes (Tr. 133, 138-139, 164-200, 621-623, 709).<sup>6</sup> The driver admitted that during his journey to Washington he never checked his brakes except by visual observation (Tr. 394-396, 422). Defendant Sim Knight knew his trailer was for carrying hay or wood chip products only (Tr. 340-342, 441-442). He admitted an absence of information about his business, transportation under I.C.C. licensing rules and requirements (Tr. 342, 427-430). He was employed sight unseen by calling a certain telephone number. His only pay was an advance of \$75 left for him at a Portland service station (Tr. 233, 339-340, 350-355, 358-362, 382-387, 428-433). And other evidence showed defendant Sim Knight to be wanting

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<sup>6</sup> The record contains evidence that operators of trucks of I.C.C. authorized carriers are trained to be constantly alert to the condition of their brakes (Tr. 554-566).

in knowledge as to proper truck driving, such as the correct starting gear for descent of a hill marked with a sign warning truckers of a steep grade (Tr. 119-367-368, 373-375, 423-425, 573, 716-717).

Witnesses expert in interstate commerce carrier matters testified that unlicensed, unauthorized carriers have marginal or unprofitable operations on account of their low, business procuring rates, and consequently soon quit (Tr. 269-270, 275, 648-657). Defendant Transport Supply Company proved no exception to the rule. The earliest record indication of its existence is approximately November 23, 1963, when employed by appellant at an unlawful, cut-rate to haul steel products to Portland from Los Angeles (Ex. 6A; Tr. 20, 277). Shortly after December 9, 1963, the date of appellees' accident, defendant Transport Supply Company cancelled its telephone and suspended its activities (Exs. 6C, 6D; Tr. 382-383). Defendant Transport Supply Company never did have a business address, operating out of Post Office box. It never was listed in the Portland telephone directory. Long-time employees of regular, legitimate carriers never heard of defendant Transport Supply Company until this action was started (Ex. 6D, Tr. 338-340, 382-383, 432-433, 449).<sup>7</sup>

Appellant engages in extensive interstate and intra-state shipments of its steel products, some 400 per month (Ex. 7; Tr. 452, 611). In view of appellant's experience and the general knowledge of steel ship-

<sup>7</sup> There are only 16-18 specialty carriers and a few general commodity carriers on the west coast authorized to haul steel rails and bars interstate (Tr. 290).

pers, the jury had sufficient evidence to decide appellant knew defendant Transport Supply Company was wholly incompetent to carry appellant's steel in interstate commerce (Tr. 271-275, 648-651). Additionally, the tractor-trailer in question was actually loaded under the supervision of appellant's employees. Whatever the relationship of defendant Transport Supply Company and defendant Sim Knight,<sup>8</sup> appellant saw and used the obviously unsafe hay truck. (R. 112-114; Tr. 446-448.)

### SUMMARY OF ARGUMENT

This is a fact appeal and the jury has resolved the facts in favor of appellees (R. 176-181). Appellant is liable because it was negligent in hiring defendant Transport Supply Company to carry appellant's steel goods, and that negligence proximately caused appellees' damages. Further, appellant is liable, as the jury held, with ample record support, because appellant willfully or wantonly violated the interstate commerce act, to appellees' detriment.

The issues argued by appellant are fictitious or erroneous. No one claims a principal is liable for his independent contractor's negligence (App. Br. 30-33). Appellees do contend, however, appellant is liable on its own negligent selection of an independent contractor. Appellees also contend Congress enacted 49 U.S.C.A. § 322(c) to protect or otherwise benefit the public, and appellant is wrong in its argument to the contrary. (App. Br. 50-66.)

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<sup>8</sup> Defendant Sim Knight testified he was an employee of defendant Transport Supply Company (Tr. 430).

## ARGUMENT IN SUPPORT OF JUDGMENT

### A. Appellant Negligently Utilized an Incompetent Carrier

The Restatement of Torts, 2d Ed., § 411, p. 376, declares appellant's duty at the time it shipped the load of steel rails and bars in the following language:

An employer is subject to liability for physical harm to third persons caused by his failure to exercise reasonable care to employ a competent and careful contractor

- (a) To do work which will involve a risk of physical harm unless it is skillfully or carefully done, or
- (b) To perform any duty which the employer owes to third persons.

The American Law Institute's comment on that section reads (pp. 376-377) :

The words "competent and careful contractor" denote a contractor who possesses the knowledge, skill, experience and available equipment which a reasonable man would realize that a contractor must have in order to do the work which he is employed to do without creating unreasonable risk of injury to others, and who also possesses the personal characteristics which are equally necessary.

There are cases that hold motor carrier freight transportation involves considerable highway danger. *Eli v. Murphy* (Cal.), 248 P. 2d 756 (1952); *Venuto v. Robinson* (C.A. 3), 118 F. 2d 679, 682-683 (1941); *Berry v. Keeler* (Mass.), 76 NE 2d 158, 164 (1947); *Hodges v. Johnson* (D.C., Va.), 52 F. Supp. 488, 490 (1943); and *Lewis v. Younger* (Ill.), 138 NE 2d 696 (1956). See, too, *N.L.R.B. v. U.S. Truck Co., Inc.* (C.A.6), 124 F.

2d 887 (1942). Obviously highway users are especially endangered whenever huge tractor-trailers, fully loaded with steel, have unsafe equipment, inadequate brakes or incompetent drivers.

The Restatement of Torts, 2d Ed. § 411, page 376, 377, cites an example of liability on all fours with the case at bar:

The A Company, engaged in logging operations, hires B Company to haul large logs over the public highway. With the exercise of reasonable care in making inquiry A Company could, but does not, discover that B Company's only available equipment consists of converted lumber trucks unsuitable for hauling such large logs in safety and on which the logs cannot be securely fastened. While such a truck of B Company is hauling the logs, they displaced while rounding a curve, and one of them falls upon the passing automobile of C, injuring C. A Company is subject to liability to C.

The law of the state of Washington, which the trial judge followed, has long recognized liability predicated upon the failure of a principal to use care in employing an independent contractor to do work dangerous unless carefully performed. *Richardson v. Carbon Hill Coal Co.* (Wash.), 32 P. 1012 (1893); *Green v. Western America Co.* (Wash.), 70 P. 310 (1902). The text writers cite the former case as indicating Washington's adherence to the majority rule of liability for negligent selection of an independent contractor. Prosser on Torts, 3rd Ed. § 70, pp. 480-481; Annotation, 30 ALR 1502, pp. 1438-1540. For other Washington cases recognizing instances of liability for work of independent contractors, see *H. W. Van Slyke*

*Warehouse Co. v. Vilter Manufacturing Co.* (Wash.), 291 P. 1103 (1930); *Amann v. Tacoma* (Wash.), 16 P. 2d 601 (1932); and *Blancher v. The Bank of California* (Wash.), 286 P. 2d 92 (1955).

The rule of liability for negligent selection of an independent contractor is almost universally followed. *Evans v. Allstate* (La.), 194 So. 2d 762 (1967); *Eitel v. Times, Inc.* (Ore.), 352 P. 2d 485 (1960); *Mooney v. Stainless, Inc.* (C.A.6), 338 F. 2d 127 (1964); *Berquist v. Penterman* (N.Y.), 134 A. 2d 20 (1957); *Matanuska Electric Assoc. v. Johnson* (Alaska), 386 P. 2d 698 (1963); *Skidmore v. Haggard* (Mo.), 110 SW 2d 726 (1937); *Carr v. Merrimack Farmers Exchange, Inc.* (N.H.), 146 A. 2d 276 (1958); *Ozan Lumber Company v. McNeely* (Ark.), 217 S.W. 2d 341 (1949); *Joslin v. Idaho Times Publishing Co.* (Ida.), 91 P. 2d 386 (1939); Annotation, 8 ALR 2d 267; 27 Am. Jur., Independent Contractors, § 28, p. 507; 2 Harper & James on Torts, § 26.11, p. 1395, 1405; 57 C.J.S., Master & Servant, § 592, p. 368; Shearman & Redfield on Negligence, Rev. Ed., Vol. 1, § 174, p. 411. Many supporting cases go to the precise question we have here: that is, *Risley v. Lenwell* (Cal.), 277 P. 2d 897 (1954) involves the negligent selection of a logging truck operator with defective equipment; *Carr v. Merrimack Farmers Exchange, Inc.* (N.H.), 146 A. 2d 276 (1958), involves the negligent engagement of a hay truck which was precariously loaded; *Ozan Lumber v. McNeely* (Ark.), 217 S.W. 2d 341 (1949), deals with the negligent retention of a log truck driver who was reckless; *Ellis & Lewis v.*

*Warner* (Ark.), 20 S.W. 2d 320 (1929), involves the careless keeping of a young and inexperienced gravel truck operator; and *Joslin v. Idaho Times Publishing Company* (Ida.), 91 P. 2d 386 (1939), concerns the negligent retention of a person to operate a vehicle to deliver papers.

Actual knowledge of incompetency of the independent contractor, although proved in the case at bar, is not a requirement. See *Joslin v. Idaho Times Publishing Company* (Ida.), 91 P. 2d 386 (1939), where the court holds it is a duty upon the principal to inquire into the competency of his independent contractor. Accord: *Carr v. Merrimack Farmers Exchange, Inc.* (N.H.), 146 A. 2d 276 (1958).

Without question defendant Sim Knight's truck involved a risk to appellees and others the whole of the journey to Tacoma from California. Without question the jury properly concluded appellant was negligent in hiring defendant Transport Supply Company, an unqualified carrier, and in utilizing the incompetent defendant Sim Knight's unsafe rig to haul appellant's steel. Without question the jury correctly decided proximate cause against appellant; that had it exercised any care whatsoever and employed a legitimate, qualified carrier, the quality of that carrier's equipment and driver would have been such the accident would not have occurred. *Risley v. Lenwell* (Cal.), 277 P. 2d 897 (1954).

#### **APPELLANT'S VIOLATIONS OF STATUTORY LAW HELPED CAUSE THE ACCIDENT**

49 U.S.C.A. § 322(c) provides in pertinent part:

Any person, whether carrier, shipper, consignee or broker, or any officer, employee, agent or representative thereof, who shall knowingly . . . . solicit, accept, or receive any rebate, concession, or discrimination in violation of any provision of this chapter, . . . or by any other means or device, shall knowingly and wilfully assist, suffer or permit any person or persons, natural or artificial, to obtain transportation of . . . property subject to this chapter for less than the applicable rate, fare, or charge, or who shall knowingly and wilfully by any such means or otherwise fraudulently seek to evade or defeat regulation as in this chapter provided for motor carriers or brokers, shall be deemed guilty of a misdemeanor.

Appellant's violation of this statute is practically conceded (Ex. 12D; R. 114; Tr. 509, 536). Appellees contend violation of the statute constitutes negligence per se. To establish negligence per se, appellees showed they were within a class the statute was designed to protect, and the hazard created by appellant was one the statute was designed to guard against. *Currie v. Union Oil Co.* (Wash.), 307 P. 2d 1056 (1957).

An objective of the regulation by Congress of interstate carriers, through the I.C.C., is public safety. The preamble of the 1940 amendment to the Interstate Commerce Act provides:

It is hereby declared to be the national transportation policy of the Congress . . . to promote safe . . . service . . . in transportation and among the several carriers.<sup>9</sup>

In 49 U.S.C.A., § 304(a) 1, 2 and 3, the I.C.C. is charged with establishing "safety of operation." Although not the precise issue involved, *U.S. v. E.*

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<sup>9</sup> 49 U.S.C.A. Historical Note, p. 9.

*Brooke Matlack, Inc.* (D.C. Md.), 149 F. Supp. 814, 820 (1957), recognizes the provisions of U.S.C.A. Title 49 as having "public safety objectives." It is manifest, then, that one of the purposes of Congressional regulation of interstate motor carriers is to guard against unnecessary traffic hazards, such as defendant Sim Knight's truck, to other users of the highway, including appellees.

Washington follows the rule that violation of a statute or ordinance requiring a license to operate a motor vehicle is negligence per se, but such negligence must be a causal factor in the injury in order to be a basis of recovery to the injured. Thus, generally, that one without a driver's license becomes involved in an auto accident does not render him liable, the want of a license not being a proximate cause. *Switzer v. Sherwood* (Wash.), 141 Pac. 181 (1914); *Wehs v. Watson* (Wash.), 203 P. 2d 350 (1949).

But the supreme court of Washington further recognizes that driving in violation of a licensing statute may be a proximate cause of injury. In *White v. Peters* (Wash.), 329 P. 2d 471 (1958), one of the plaintiffs, an amputee, drove a car contrary to his restricted driver's license, which required that any car he operated be equipped with a hand throttle. The court held that whether he was contributorily negligent was a jury question. At 329 P. 2d 471, 474 appears:

Plaintiff White's noncompliance with the requirements of his restricted driver's license may or may not have been a factor contributing to the accident. Whether his noncompliance is a proxi-

mate cause of the accident is a jury question in the circumstances of this case.

Thus, the critical question seems to be whether there is a reasonably direct relationship between the violation of a licensing provision and the accident.

Here at bar the relationship lies in appellant's use of a woefully unsafe truck of an unauthorized cut-rate interstate carrier. The provision of Title 49 of U.S.C.A., and the I.C.C. regulations pursuant thereto, comprise a whole complex of requirements for maintenance and inspection of motor carriers to insure their movement in interstate commerce with safety (Tr. 648-666; Tr. 880-882). The law provides for minimum tariffs to render certain, among other things, a sufficient return that interstate motor carrier equipment can be adequately and safely maintained and operated. When appellant, as the shipper, and defendant Transport Supply Company, as the carrier, entered into the arrangement for the low cost and unlicensed interstate movement of appellant's steel products, the result was foreseeable if not inevitable. The jury was well within its province in finding appellant's shipment via an unlicensed carrier at a cut-rate charge, a statutory violation, aided and abetted the use of an unqualified driver or substandard equipment, proximately resulting in injury to appellees. As previously discussed, it is the same as in *White v. Peters* (Wash.), 329 P. 2d 471 (1958), where the jury was permitted to find the driving of a standard automobile by an amputee without a license to do so was one of the causes of the accident.

## ARGUMENT ANSWERING APPELLANT

### I. Appellant Raises an Untimely Issue

A study of appellant's exceptions to instructions given and refused shows it neither requested the court to rule as a matter of law defendant Sim Knight was an independent contractor of defendant Transport Supply Company, nor submitted an appropriate jury instruction to that effect (Tr. 913-921). Appellant's present theory that defendant Sim Knight was not an employee of defendant Transport Supply Company was not mentioned to the trial court.<sup>10</sup> In fairness, and in law needing no citation, appellant's argument cannot be considered at this late date.

Regardless, appellant's factual background for its new argument is faulty. The record is replete with evidence indicating defendant Sim Knight was an employee of defendant Transport Supply Company.<sup>11</sup> Nor is the legal status of defendant Sim Knight at the time of the accident of real consequence. Defendant Transport Supply Company was attempting to carry on the function of a franchised carrier author-

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<sup>10</sup> Appellant's Brief, pp. 30-33. An instruction was proposed (and the court gave one) to the effect that defendant Sim Knight was an independent contractor in his relationship to appellant. (Tr. 890, 919-920), but that would have no bearing on whether he was defendant Transport Supply Company's employee or independent contractor.

<sup>11</sup> For instance, defendant Transport Supply Company sent defendant Sim Knight to Sacramento (Tr. 338). He was instructed to call home before the return trip (Tr. 353). He did telephone and was directed to go to San Leandro (Tr. 355-356). Following the accident defendant Sim Knight called defendant Transport Supply Company for instructions (Tr. 428-429). He thought he was using defendant Transport Supply Company's license (Tr. 428-429, 441). Perhaps most important, defendant Sim Knight considered himself an employee of defendant Transport Supply Company, and so informed the federal government (Tr. 429-430).

ized to operate in interstate commerce by the I.C.C. (Tr. 701). A franchised carrier may not delegate its duties to an independent contractor and escape liability for the latter's negligence.<sup>12</sup> Thus in *Eli v. Murphy* (Cal.), 248 P. 2d 757, 758 (1952), the court said:

C.M.T., operating as a highway common carrier, is engaged in a business attended with very considerable risk . . . .

The legislature has, however, classified highway common carriers, such as C.M.T. apart from others, and by so doing has indicated special concern with the safety of their operations . . . .

It is our conclusion that any trucking company, upon becoming a public utility under the Public Utility Act, should be expected to exhibit a high degree of performance in the field of safety and should expect to be required to observe rigid safety rules and regulations . . . .

In view of the more extensive and regular operations of highway common carriers as compared with others, the Legislature could reasonably conclude that the safety of their operations is of special importance and legislate accordingly. Highway common carriers may not, therefore, insulate themselves from liability for negligence occurring in the conduct of their business by engaging independent contractors to transport freight for them,

Appellees would further submit the legal status of defendant Sim Knight became moot when employees of appellant accepted defendant Sim Knight's truck by supervising the loading operation (R. 114; Tr. 445-446). Appellant therefore knew the type of equipment

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<sup>12</sup> Restatement of Torts, 2d Ed. § 428, p. 420.

being utilized to haul its steel to the state of Washington and also knew the equipment bore no I.C.C. numbers, which numbers would show the truck met I.C.C. safety regulations. The I.C.C. rules governing maintenance and safe operation of motor trucks were submitted to the jury (Tr. 880-882). Appellant's negligence, in part, is predicated upon that direct sanction of defendant Sim Knight and the use of his unsafe truck to haul appellant's goods.

## II. Appellant Caught Red-Handed

Appellant states the law as imposing

. . . liability on the employer for the harm proximately resulting from failure to select a competent independent contractor,

and argues for actual notice of prior incompetency.<sup>13</sup> Appellant ignores its illegal, rate-cutting contracts with defendant Transport Supply Company extending over the two weeks before the accident involving appellees (Exs. 6A, 6B; Tr. 19-23, 276-281). In that unregistered, "fly by night" motor carriers have but short lives (Tr. 649-651), notice of two weeks of defendant Transport Supply Company's lack of certification was more than ample and should foreclose the issue.<sup>14</sup>

Under appellant's theory a shipper can with im-

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<sup>13</sup> Appellant's brief, p. 34. Appellant only half states the law. See Annotation 8 ALR 2d 267.

<sup>14</sup> *Moore v. Roberts* (Tex.), 93 S.W. 2d (1936), cited by appellant (App. Br. 38) is inapplicable because no rate cutting concession was involved. *Mooney v. Stainless, Inc.* (C.A. 6), 338 F. 2d 127 (1964), not a commerce or trucking case, is of no assistance as there the proof of improper equipment was wanting. As the equipment of the independent contractor was satisfactory, advance notice would have availed nothing.

punity hire a newly activated illegal and unsafe carrier because of no prior history of accidents and/or incompetency (App. Br. 33-43). Adoption of such a rule would merely serve to license shippers and illegal carriers to flaunt the I.C.C. and its safety rules and regulations. Because defendant Transport Supply Company was unregulated and new, though having had several weeks of dealings with appellant, the court properly accepted testimony of experts to the effect that unlicensed carriers have faulty help and equipment, haul at illegal, rate-cutting rates and soon go out of business because of an accident or insolvency; that these characteristics are generally known to those engaged in interstate shipping (Tr. 640-666). The evidence shows beyond doubt that the haul of appellant's steel to Seattle was at a rate less than legal (R. 112-114; Tr. 509-510, 536), and appellant knew of activities of unlawful carriers (Tr. 536). The jury therefore had a right to total two and two at four; that is, that appellant knew or should have known defendant Transport Supply Company was without competency as to equipment or operator, or both.

### **III. Appellant Foiled by the Interstate Commerce Act**

Appellant contends the I.C.C. has exclusive jurisdiction in the field of enforcement of federal law regulating interstate motor carriers (App. Br. 48). The proposition is unsupported by case law or common judgment. Obviously, the I.C.C. police force thereby needed to patrol the nation's highways would stagger the pocketbook of Congress. As with most criminal statutes, violation of 49 U.S.C.A. § 322(c) gives

rise to a civil action, as well as to government prosecution. A comparable analogy is the Public Accommodations Act of Washington, RCW 9.91.010. The supreme court of that state has held such law, while penal in form, is also remedial in nature and effect, giving the wronged party his right to sue for civil damages. *Anderson v. Pantages Theatre Co.*, (Wash.), 194 P. 813 (1921); *Browning v. Slenderella Systems* (Wash.), 341 P. 2d 859 (1959).

The claim of appellant of ignorance about its carrier's illegal activities is somewhat hollow (App. Br. 54-57). Appellant commenced using defendant Transport Supply Company's cut-rate service November 23, 1963 (Ex. 6A), affording ample opportunity to inquire about the carrier prior to the December 7, 1963 shipment that injured appellees (Exs. 5A, 6C). However, it is clear from the evidence the lack of defendant Transport Supply Company's certification was of no concern to appellant (Tr. 442, 484, 487, 518-520, 536). Appellant's callous disregard for the I.C.C. and its rules and regulations imputes knowledge of the illegality of defendant Transport Supply Company. *U.S. v. Gunn* (D.C. Ark.), 97 Fed. Supp. 476 (1950). See also *U.S. v E. Brooke Matlack, Inc.*, (D.C. Md.), 149 F. Supp. 814 (1957); *Steere Truck Lines, Inc. v. U.S.* (C.A. 5), 330 F. 2d 719 (1964).

From the evidence the jury undoubtedly concluded appellant knew the I.C.C. never certified defendant Transport Supply Company. Regular interstate shippers hiring new, unknown carriers to haul their

goods always check them out (Tr. 273).<sup>15</sup> Appellant customarily uses Wigle and Larimore, a San Francisco freight rate bureau, which could well (and probably did) advise appellant about defendant Transport Supply Company (Tr. 490). A telephone call to the local I.C.C. office would develop the same information within two or three minutes (Tr. 659-660). There are only 18 carriers or so qualified to carry steel rails and bars in interstate commerce on the West Coast (Tr. 290). Considering appellant's 400 outbound shipments per month (Tr. 511) and the need for special trucking equipment for its steel products (Tr. 526-527), it takes little acumen to conclude that if appellant made no inquiry about the carrier, it is because appellant knew at the outset defendant Transport Supply Company was illegitimate.<sup>16</sup>

That appellant was innocent of seeking an unlawful

<sup>15</sup> Jack L. Stewart of the Willamette Tariff Bureau testified:

Q. (Mr. Hulscher) Are you familiar with the practice in the shipping industry when shipper hire new and unknown motor carriers to haul their goods?

A. Yes, sir.

Q. And would you tell us what that practice is.

A. Well, quite often when a carrier is granted new interstate authority and is unknown to the shipping industry, we will receive for the first few months at least the man is in business, a number of calls from shippers inquiring as to the lawful authority that the man has and has been granted by the ICC and also as to what tariffs he may subscribe to. Now, we get these calls not only for Willamette Tariffs, we also maintain, as I previously stated, a large file of existing tariffs, quite often the shippers know that these tariffs are available in our office, and they will call us inquiring about a carrier even though he is not a party to Willamette Tariff (Tr. 273.)

<sup>16</sup> The jury was likewise entitled to consider the warning defendant Sim Knight imparted to appellant when he showed up with his old, broken down hay rig at appellant's San Leandro warehouse without I.C.C. identification or other markings (Ex. 12D; Tr. 266).

rate concession from its carrier also strains credulity. According to the evidence, steel shippers just don't forward their products in interstate commerce without knowing what rates they are paying. (Tr. 292-293.)<sup>17</sup> Appellant concedes its price for the steel goods included the motor freight rate to Seattle (Tr. 506). That rate should have been \$1.00 per hundredweight, but appellant paid substantially less (R. 113; Tr. 509, 536), thus giving appellant an edge on competition in a new area it was entering, the Pacific Northwest (Tr. 504). The jury could only decide appellant knowingly obtained its unlawful rate on the shipment injuring appellees, for that is the history of each of the half dozen movements defendant Transport Supply Company made for appellant (Exs. 6A, 6B, 6C, 6D). Further, before the jury was the legal requirement that interstate freight invoices be billed and paid within seven days of a shipment. A shipper violating the law is subject to fine. (Tr. 279.) Appellant's November 23, 1963, shipment via defendant Transport Supply Company should have been paid by the 1st or 2nd of December, 1963. Appellant contends it was not invoiced for an additional two weeks. The jury could infer that by the time defendant Sim Knight arrived, appellant would have been inquiring into the circumstances of its carrier unless, of course,

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<sup>17</sup> Appellant wrongly claims the tariffs of lawful carrier are identical. Thus, the rates of members of Pacific Inland Tariff Bureau members, regular route regulated carriers are generally higher in tariffs of members of the Willamette Tariff Bureau, irregular route carriers. (Tr. 300-307.)

appellant already possessed that information.<sup>18</sup>

Appellant relies on several Oklahoma and Georgia cases, as well as upon the attitude of its employees, that once the goods are surrendered to a carrier, regardless of competency, the shipper is relieved of liability (App. Br. 49, 59-64; Tr. 537-538). In none of appellant's cases, however, did the court find the charge for the transportation was less than the lawful rate. The prohibition against rate-cutting is the essence of 49 U.S.C.A. § 322(c). Moreover, the ruling in *Marion Machine Foundry v. Duncan* (Okla.), 101 P. 2d 813 (1940); and *Barsh v. Mullins* (Okla.), 338 P. 2d 845 (1959), is predicated on law which, unlike the state of Washington, holds the negligent selection of an incompetent independent contractor is not ground for liability of the principal (the contractee). In *Marion Machine Foundry v. Duncan* (Okla.), 101 P. 2d 813 (1940) appears:

In some jurisdictions there is an established rule to the effect that if one would avoid liability for the negligence of his independent contractor toward a third party he must exercise reasonable care in his selection of a person in this capacity . . . *But so far as we know this court has had no occasion to apply that rule.* (Emphasis supplied.)

*DeBord v. Procter & Gamble* (CA 5), 146 F. 2d (1944), applying Georgia law, cites as its controlling

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<sup>18</sup> Appellant seems to admit the invoice of defendant Transport Supply Company for the December 3, 1963, shipment (Ex. 6B) was delivered appellant four days later (App. Br. 50). Heedless of this notice, appellant continued to ship with defendant Transport Supply Company (Ex. 6D), thus seriously questioning appellant's contention it knew nothing before defendant Sim Knight's accident (App. Br. 50).

authority *Marion Machine Foundry v. Duncan* (Okla.), 101 P. 2d 813, 815 (1940).

If appellant is contending the law of Washington on liability for negligent selection of an independent contractor is the same as that of Oklahoma and Georgia, it is submitted such contention is patently wrong. The law of Washington has been otherwise since 1893. *Richardson v. Carbon Hill Coal Co.* (Wash.), 32 P. 1012 (1893); *Green v. Western American Company* (Wash.), 70 P. 310 (1902); and see *H. W. Van Slyke Warehouse Co. v. Vilter Mfg. Co.* (Wash.), 291 P. 1103 (1930). See also Prosser on Torts, 3rd Ed., §70, p. 480-481.

With respect to appellant's contention its violation of 49 U.S.C.A. § 322(c) was not the proximate cause of the accident (App. Br. 57-66), the case at bar is not akin to driving a car without a license. Admittedly the want of a driver's license, which is obtainable upon application, is not the proximate cause of any accident. But here at bar defendant Transport Supply Company and defendant Sim Knight did not qualify for I.C.C. certification; it was not available to either. Appellees do concede it is within the realm of possibility defendant Transport Supply Company, upon application and compliance with federal law and I.C.C. safety regulations, could have been certified. For certain, had defendant Transport Supply Company been properly licensed, there would have been good equipment and an adequate driver,<sup>19</sup> no need to

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<sup>19</sup> The trial court instructed the jury in effect that the I.C.C. required safe tractor-trailers with good and adequately maintained brakes and competent drivers (Tr. 880-882).

cut rates and no accident. Hence, the jury rightly found appellant's violation of 49 U.S.C.A. § 322(c) aided in putting defendant Transport Supply Company's unsafe trucking equipment on the highway, to the severe detriment of appellees.

#### **IV. Claimed Trial Errors Are Picayune**

The court below did not require the jury to find appellant had actual knowledge of its violation of 49 U.S.C.A. § 322(c). The court instructed the jury it sufficed to establish negligence if appellant should have so known (Tr. 893-894). A case in point is *U.S. v. Gunn* (D.C., Ark.), 97 F. Supp. 476 (1950). There defendant Gunn had motor trucks he "leased" to defendant Ozark Packing Co., but defendant Gunn hired and controlled the drivers. Defendant Ozark Packing Co. paid a lesser rate than charged by carriers with I.C.C. permits. Defendant Gunn was not licensed, but there was no evidence that fact was known to defendant Ozark Packing Co. Upon an indictment being filed, defendant Gunn pleaded *nolo contendere*. The question was whether defendant Ozark Packing Co. was guilty of violating 49 U.S.C.A. §§ 309(a) and 322(a). The evidence further disclosed defendant Ozark Packing Co. was primarily interested in having its goods transported at a rate cheaper than it would pay a valid carrier. In finding against defendant Ozark Packing Co., the court said (97 F. Supp. 476-480):

The defendant, Ozark Packing Co. is presumed to have a practical knowledge of the law commensurate with its duties, the non-discharge of which

may constitute an offense. A sane person who commits a wrong is bound to know that the wrong is subject to penal consequences. If the wrong is malum prohibitum, it should be known by the person for it is his duty to know what the law prohibits. Otherwise, no statute of this nature could be enforced. . . .

There is no doubt that the defendant, Ozark Packing Co., intended to do what it did do. It knowingly entered into the arrangement with the defendant, Clifford C. Gunn, and to permit the defendant to escape punishment would be against the policy of the law, and the law treats such a defendant as if he were cognizant of the effects of which he did. Accepting the testimony of Mr. Kimbrough, the president and manager of the defendant corporation, to the effect that he was not advised of the status of his co-defendant, Clifford C. Gunn, yet this is not an excuse, because his ignorance is the result, to say the least, of negligence on his part and, since the act committed is made an offense irrespective of his intention at the time, then his ignorance that the act would constitute an offense is no defense. *The defendant corporation should have known the facts and, even though it may not have known all the facts, yet it is charged with the facts and its failure to know the facts is not a defense.* (Emphasis supplied.)

It is also submitted there is a difference between a shipper who simply engages a carrier who has no I.C.C. certificate, as in the cases cited by appellant, and a shipper, as at bar, who not only engages such a carrier but also pays a rate less than that allowed to authorized carriers. The combined offenses, when committed with actual or constructive knowledge, vi-

olate 49 U.S.C.A. § 322(c), and that is all the jury below was advised (Tr. 893-894).

Nor is appellant's complaint on the admission of testimony about the reputation of illegal carriers well taken (App. Br. 69-72). Mr. Felix Baker, appellant's salesman who placed the order shipping the mine rails and bars with defendant Transport Supply Company, was aware there were uncertified carriers and knew they constitute a law enforcement problem (Tr. 535-538). In that Mr. Frank E. Landsburg, the former I.C.C. regional manager, merely confirmed (albeit with elaboration) the previous testimony of Mr. Baker, there can be no error (Tr. 640-666).

Appellee offered the testimony of Mr. Landsburg, and that of Messrs. Conner of Pacific Inland Tariff Bureau (Tr. 10-50) and Jack T. Stewart of the Willamette Traffic Bureau (Tr. 267-323), to show that among those engaged in heavy interstate shipping, illegal carriers were reputed to exist, carriers which charged cut rates and utilized unsafe equipment and incompetent drivers. The testimony was not offered to prove defendant Transport Supply Company was an illegal carrier charging unlawful rates and operating substandard equipment. These facts were proved by direct testimony, exhibits and other evidence. That the trial court properly admitted the common knowledge testimony as an exception to the hearsay rule, to show appellant was on notice, see McCormick's Handbook of the Law of Evidence, 1954 Ed. § 299, p. 624:

The existence of a reputation, or general manifestation of belief of a large group of people as to

a particular fact, may be material, apart from the correctness of the belief. This is true, for example, when reputation that a fact exists is offered not to show the fact but to show that someone in the range of the reputation probably had knowledge of the reputed fact.

The remaining errors assigned by appellant pertain to relatively minor points and, even if well taken, would not warrant another lengthy trial where the result would be the same. The testimony about appellant's many rate concessions from defendant Transport Supply Company was not repetitive (App. Br. 72). Appellees had to prove appellant's violations of 49 U.S.C.A. § 322(c), which deals with rate-cutting, to substantiate one of their theories of appellant's liability. The trial court's charge on proximate cause, only a small part of which does appellant quote (App. Br. 74-75), is in accord with the law of Washington. The jury was told that one chargeable with negligence is liable for an injury which was reasonably foreseeable in the exercise of care (Tr. 875). But even if appellant was negligent, any independent negligence of defendant Sim Knight not foreseeable, would relieve appellant of liability (Tr. 876-877). That is all appellant's citation *Mehrer v. Easterling* (Wash.), 426 P. 2d 843 (1967), requires.

## CONCLUSION

In the main appellant's argument is based on its version of the facts.<sup>20</sup> The jury, however, decided factual questions in favor of appellees (R. 176-181).

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<sup>20</sup> Appellant's facts are not even complete. See and compare appellee's corrected appendix of all exhibits at the end of this brief.

It is submitted the verdict and judgment below should be sustained if this court finds appellees proved, as they did, appellant was negligent in hiring an independent contractor to do work involving the risk of physical harm to others unless carefully done. Only if the facts do not warrant the submission of that question to the jury will this court reach the second issue: did appellant's negligent violation of 49 U.S.C.A. § 322(c) proximately cause appellees' injuries? Here, too, the facts in evidence should impell this court to agree with the jury's decision.

Respectfully submitted,

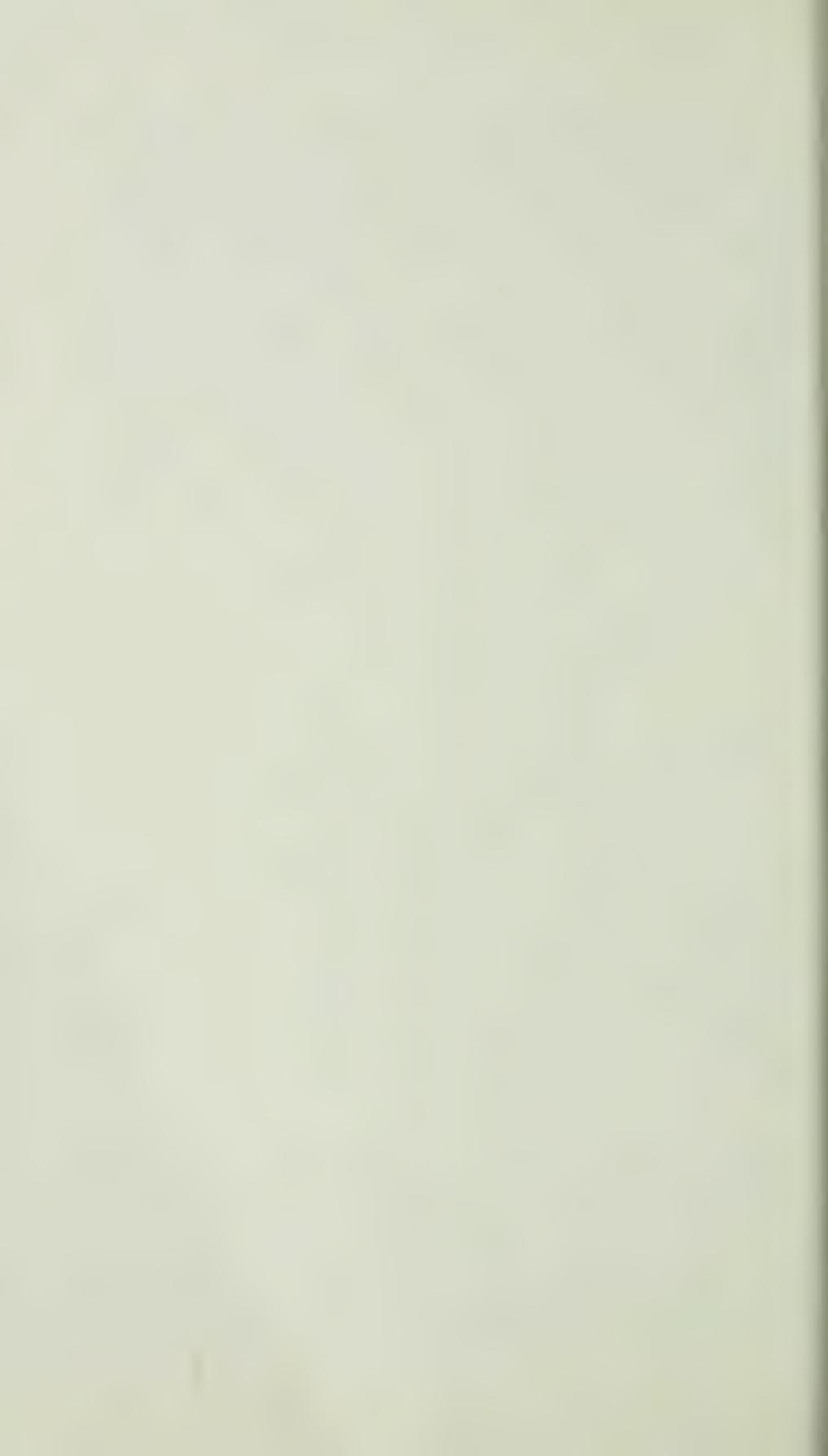
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### **CERTIFICATE OF COUNSEL**

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion the foregoing brief is in full compliance with those rules.

GERALD L. HULSCHER,  
*Attorney for Appellees*

Dated this 3rd day of June, 1968



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United States Court of Appeals  
For the Ninth Circuit

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L. B. FOSTER COMPANY, INC.  
*Appellant,*

*vs.*

MELVIN HURNBLAD, and GRACE HURNBLAD, his wife  
*Appellees,*

---

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION

---

APPELLANT'S REPLY BRIEF

---

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MU 2-2444

FILED

JUL 23 1968



United States Court of Appeals  
For the Ninth Circuit

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*Appellant,*

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# **United States Court of Appeals For the Ninth Circuit**

**L. B. FOSTER COMPANY, INC.**

*Appellant,*

vs.

**MELVIN HURNBLAD, and GRACE**

**HURNBLAD, his wife,**

*Appellees.*

**No. 22597**

**APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION**

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## **APPELLANT'S REPLY BRIEF**

---

### **I. REPLY TO APPELLEES' STATEMENT OF THE CASE**

Appellees open their brief with the charge that appellant's statement of the case was made in bad faith. The allegation is groundless, and tasteless. Appellant set out in seven pages (App. Br.\* pp. 2-8) the facts relevant to the issues presented for review in this appeal fully, fairly and concisely. Since this appeal turns ultimately and singularly on the question of liability of L. B. Foster Co., Inc., only those facts necessary for consideration of that issue are included in appellant's statement of the case. However, appellees add to their version of the case (Ans. Br.

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\*Herein App. Br. will indicate Appellant's Opening Brief and Ans. Br. will indicate Appellees' Answering Brief.

pp. 3-12) minutia<sup>1</sup>, irrelevancies<sup>2</sup>, and surprisingly, in light of their charge of bad faith, conclusions and argument based on their version of the evidence.<sup>3</sup> It goes without saying that conclusions drawn by one party, and argument based thereon have no place in the statement of a case. The duty of an appellate advocate is to present his case in the best ethically possible light, but he violates this duty when he attempts to introduce his own conclusions and argument as fact.

Appellees (Mr. and Mrs. Melvin Hurnblad hereinafter referred to in the singular) also include in their statement of the case an allegation of an attempt by appellant (L. B. Foster Co., Inc. hereinafter referred to as Foster) to deliberately mislead this court (Ans. Br. p. 4). Hurnblad quotes out of context a portion of one sentence appearing on page 38 of Foster's brief. He fails to quote the succeeding sentence, (page 38)

“However, even assuming that Transport Supply was not properly licensed to engage in

<sup>1</sup>Note on page 3 alone: “1961 Ford”; “sitting in the right front seat”; “controlled by a standard overhead red and green traffic signal.”

<sup>2</sup>Appellees go on for four pages (pp. 8-11) reciting everything in the record which would possibly indicate incompetence on the part of *Sim Knight*. This latter material is presented notwithstanding the fact that the only issue presented to the jury by the court was that of the incompetence of *Transport Supply* (R. 164 & 180), and that Appellant's argument was directed specifically to the lack of proof of incompetency of *Transport Supply*.

<sup>3</sup>Appellees' conclusions disguised as facts *inter alia*: last sentence of incomplete paragraph page 10; the sentence beginning on page 11 running over to page 12. However, the most serious indiscretion occurs on the top of page 5 where Appellees attempt to create the inference that Foster stipulated that it knew at the time of the shipment that the rate involved was below the minimum. Reference to the Pretrial Order (R. 114) shows clearly and singularly that Foster did ship and that it was subsequently billed at an amount less than the minimum. Nothing whatsoever was stipulated and Hurnblad did not prove anything as to Foster's knowledge of the rate prior to the shipment.

an interstate haul, this does not constitute evidence of incompetency."

which negates the effect of Hurnblad's quoted squib. In addition, it should be noted that in order to substantiate his position to any extent, Hurnblad cites to a portion of the transcript which was not even ordered until after Foster's opening brief was filed. Foster had ordered that the transcript should contain "all testimony on the issue of liability relating to all the defendants and the additional defendants" (R. 194). The opening brief was prepared in reliance on the assumption that a conforming transcript had been provided. However, on June 20, 1968, some 14 days after Foster's brief was filed, the District Court forwarded to the Clerk of this Court an Addendum to the Transcript which had been filed only that day (Letter from Harold W. Anderson to William B. Luck, June 20, 1968).

Hurnblad's groundless allegations of bad faith and deliberate misrepresentation need no further answer.

## **II. REPLY TO HURNBLAD'S ARGUMENT IN SUPPORT OF JUDGMENT**

### **A. FOSTER INCURRED NO LIABILITY BY CONTRACTING WITH TRANSPORT SUPPLY**

Appellee Hurnblad begins his argument with a quotation from Restatement (Second), Torts §411 setting forth part of the rule, part of the comment and one of the examples. He concludes from this that the act of shipping done herein was an act fraught with inherent danger. This bare conclusion should be compared to Prosser, Torts §70 at p. 486 (3rd ed.

1964) where in discussing the rule that an employer may be liable for the negligence of an independent contractor hired to do a job he states:

*"One who hires a trucker to transport his goods must, as a reasonable man, always realize that if the truck is driven at an excessive speed, or with defective brakes, some collision or other harm to persons on the highways is likely to occur. But this is not 'inherent danger' as the courts have used the term; and for such more or less usual negligence the employer will not be liable."* (Emphasis added.)

The author distinguishes this situation from Hurnblad's example:

"When the trucker is to transport over the highway giant logs which require special care to fasten them securely, there is obviously a special danger, and the exception applies."

In this single sentence Prosser points up the derth of reasoning which inflicts all of Hurnblad's argument. Here Hurnblad attempts to take a rule of narrow, specific, pinpoint accuracy and turn it into an all covering blanket. This would make every employer an insurer of each independent contractor which he hires, no matter what the job or what the circumstances. Appellees' protest notwithstanding such is not the law.

## **1. HURNBLAD FAILS TO DISCERN THE WASHINGTON RULE ON THIS QUESTION**

Hurnblad sets out the rule that an empoyer can be held liable for employing an incompetent, and for this he cites some five Washington cases. Foster does not quarrel with this rule. (See App. Br. p. 34.)

Moreover, Hurnblad fails to apprise this court of anything about these cases; he does not quote them as giving voice to any fundamental rationale but apparently is content that the mere naming of the cases will suffice.

The first case cited by Hurnblad is *Richardson v. Carbon Hill Coal Co.* (Wash.), 32 Pac. 1012 (1893) which is officially reported at 6 Wash. 52. It was treated in depth at p. 35 of Foster's brief. Here, while discussing the liability of an employer for engaging an incompetent, the court laid clear a distinction to be drawn between "negligence" and "incompetence." In *Richardson* the court clearly stated that negligence refers to the particular act which gave rise to the instant lawsuit; whereas competency or incompetency refers to the characteristics displayed by the individual antecedent to the act involved.

Hurnblad cites *Green v. Western America Co.*, 30 Wash. 87, 70 Pac. 310 (1902). A portion of the opinion is quoted at p. 36 of Appellant's Brief. This case held that there exists a presumption that an employer has exercised proper care in selection of his help. It further stated that in order to overcome this presumption the attacking party must show either that the employer knew in fact that the contractor was incompetent, or that the contractor had demonstrated his antecedent incompetence by specific acts of such a nature, character and frequency that the employer must have had them brought to his attention.

Appellee Hurnblad also cites *Amann v. Tacoma*, 170 Wash. 296, 16 P.2d 601 (1932). This was a case wherein a building owner had let a contract for the demolition of his building. The contractor made a sub-

contract with another contractor. In the course of demolition, the building front fell on the plaintiffs who were sitting in a parked car on the street in front of the building. On appeal the Washington State Supreme Court reversed as to the dismissal of the two contractors, but affirmed the dismissal of the owner. On the way to this conclusion of no liability on the part of the principal, the court said (16 P.2d at 607):

“Generally speaking, where the act which causes the injury is one which the contractor is employed to perform and the injury results from the act of performance and not from the manner of performance; . . . or where the work is inherently or intrinsically dangerous in itself, and will necessarily or probably result in injury to third persons, unless measures are adopted by which such consequences may be prevented; and in other like cases — a party will not be permitted to evade responsibility by placing an independent contractor in charge of the work.”

The court then noted that the injury resulted not from the act of doing the work, but from the manner in which it was done, and that the work of demolition of a building standing immediately adjacent to a public street was not inherently or intrinsically dangerous.

The other Washington cases cited by appellant are not on point: *H. W. Van Slyke Warehouse Co. v. Vilter Mfg. Co.*, 158 Wash. 619, 291 Pac. 1103 (1930), and *Blancher v. Bk of Calif.*, 47 Wash.2d 1, 286 P.2d 92 (1955).

## 2. HURNBLAD'S CASES FROM OTHER JURISDICTIONS DO NOT HELP HIS POSITION

Appellee cites some nine cases and five authorities for the proposition that an employer may be held liable for harm proximately resulting from failure to select a competent independent contractor (Ans. Br. p. 15). This seems somewhat superfluous in light of the fact that appellant conceded this point (App. Br. p. 34). Out of this mass of unnecessary authority, Hurnblad selects five cases which he describes as going to the "precise question which we have here".

The first case cited by Hurnblad is from an intermediate appellate court in California, not the California Supreme Court as appellee's form of citation would at first indicate: *Risley v. Lenwell*, 129 Cal. App. 2d 608, 277 P.2d 897 (1954). This is the giant log illustration cited by Hurnblad on page 14 of his brief, and distinguished from the case at bar by Prosser *supra* at page 4. In Restatement (Second) Torts, Reporters Notes §411 it is stated:

"Illustration 2 is taken from *Risley v. Lenwell*, 129 Cal. App. 2d 608, 277 P.2d 897 (1954)."

In addition, a reading of the case shows that it is clearly distinguishable not only on the law but on the facts. The particular piece of defective equipment used by the independent contractor had been in the employer's yard not once, as Sim Knight was, but half a dozen times over a period of some three weeks and it had been constructed with aid and material from the principal.

Hurnblad also cites *Joslin v. Idaho Times Pub. Co.*, Ida....., 91 P.2d 386 (1939). This is clearly in-

apposite as it adopts by way of dictum the minority rule which places the burden of proof on the principal. This is exactly opposite to the rule in Washington as indicated by the *Green* case which places the burden firmly on the plaintiff to come forward with a significant amount of proof in order to overcome the presumption of due care on the part of the principal. See also *Miller v. Mohr*, 198 Wash. 619, 642, 89 P.2d 807 (1939) quoted at App. Br. p. 37.

Hurnblad also cites *Carr v. Merrimack Farmers Exch.*, 101 N. H. 445, 146 A. 2d 276 (1958). Among several rulings the court made was one which held that the transportation of ten tons of hay was not an inherently dangerous activity since that term "implies work that is dangerous even when conducted with reasonable care." In addition, the court specifically refused to hold that the principal had a duty to inspect the load.

Hurnblad cites two cases from Arkansas: *Ellis & Lewis v Warner*, 180 Ark. 53, 20 S.W. 2d 320 (1929) and *Ozan Lumber Co. v. McNeely*, 214 Ark. 657, 217 S.W. 2d 341 (1949). Of significant interest is the *Ozan Lumber* case wherein the court quoted from 57 C.J.S. *Master & Servant* §592:

"The fact that a contractor is negligent in respect of the work in question raises no presumption that the employer was guilty of negligence in employing him."

The court concludes its discussion of the law in this area by quoting from the *Warner* case and then stating (217 S.W. 2d at 345):

"So here, appellant [principal] would be liable if it negligently employed Kirby [independ-

ent contractor] as an independent contractor knowing that he was a careless, reckless and incompetent truck driver or operator."

(Emphasis added).

Examination of the *Ozan Lumber* case, cited by Hurnblad on page 15 as supporting his position, shows conclusively that the rule of law developed in appellant's argument (App. Br. pp. 34-41) is the general rule in this country as well as in this jurisdiction. The vital pivotal question always comes up the same: Was the independent contractor shown to be in fact incompetent? Hurnblad had this burden of proof laid on him by the Washington cases beginning with *Richardson, supra* at p. 5 and running through *Miller, supra* at p. 8 (See App. Br. pp. 35-37). Hurnblad failed to get off ground zero in discharging this burden. All he can talk about in his argument and statement of the case is that *Knight* was incompetent. But *Knight* was not hired by Foster. Foster was not charged with negligence regarding *Knight*. The question presented was: Did Foster negligently select *Transport Supply* as an independent contractor? (R. 164 & 180) Not one iota of evidence did Hurnblad introduce concerning *Transport Supply*'s antecedent activities. He brought nothing into court which would indicate any bad habits by *Transport Supply*, but he now asks this court to hold that Foster should have known all about this non-existent incompetent activity.

**B. NO SHOWING THAT FOSTER VIOLATED ANY STATUTE OR THAT ANY STATUTORY VIOLATION WAS THE PROXIMATE CAUSE OF THE ACCIDENT**

**I. HURNBLAD PRESENTS NOTHING TO SHOW A VIOLATION OF THE STATUTE**

Hurnblad opens this portion of his brief with a groundless statement. He states (Ans. Br. p. 17) :

“Appellant’s violation of this statute [49 U.S.C.A. §322(c)] is practically conceded. (12D; R. 114; Tr. 509, 536)”

Hurnblad, by this, indicates that he has failed to take cognizance of Appellant’s Brief, pp. 45-51, where it is most emphatically and clearly shown that Hurnblad did not come forward with even a scintilla of evidence which would indicate that Foster did knowingly violate the statute. In support of this untenable statement Hurnblad cites to Exhibit 12D which showed only that Transport Supply and Sim Knight were not I.C.C. approved. He also cites to page 114 of the Record which contains some eleven admitted facts, none of which in any way treat of what knowledge Foster had. Hurnblad’s reference to page 509 is completely opaque. His reference to page 536 is equally obscure, for here Mr. Baker, a salesman for Foster, testified in response to a question from the court that he had no way of knowing whether Transport Supply was regulated, and that he would not knowingly ship by an unregulated carrier.

## 2. HURNBLAD PRESENTS NO COGENT ARGUMENT THAT HE OR HIS INJURY WERE CONTEMPLATED BY THE STATUTE

Hurnblad quotes a portion of the preamble to the 1940 Amendment to the Interstate Commerce Act. Taken out of context in the manner presented by Hurnblad, it appears that the one prime overriding purpose of the Interstate Commerce Act was safety.<sup>4</sup> However, examination of the full body of the preamble shows that it is not that simple.<sup>5</sup> A casual reading reveals some seven purposes, and a second reading reveals a total of thirteen. In addition, examination of these reveals that some of the purposes are not only not supplementary or complementary to each other, but are in direct conflict.<sup>6</sup>

From this examination it becomes clear that the Transportation Policy of the Congress is a many jumbled thing. Perhaps one of the tertiary or quaternary purposes of the statute was as Hurnblad alleges, but the primary purpose for the Interstate Commerce Act was pointed out over seventy-five years ago in *I.C.C. v. Baltimore & O. R.R.*, 145 U.S. 263 (1892):

“The principle objects of the Interstate Commerce Act were to secure just and reasonable

<sup>4</sup>Hurnblad fails to acknowledge or answer the line of cases from *I.C.C. v. Baltimore & O. R.R.*, 145 U. S. 263 (1892) to *New York v. United States*, 331 U. S. 284 (1947) (cited and quoted at pp. 55-57 of App. Br.) in which the Court consistently held that the injury to be prevented by the statute was economic injury and the group to be directly benefited was the shipping industry.

<sup>5</sup>The entire text of the Preamble is set forth in the Appendix.

<sup>6</sup>Some of the more obvious conflicts include the administration of the Act to recognize inherent advantages of each mode of transportation while at the same time attempting to preserve all the methods of transportation. In addition, economical and efficient service may very definitely be in conflict with fair wages and equitable working conditions.

charge for transportation; to prohibit unjust discriminations in the rendition of like services under similar circumstances and conditions; to prevent undue or unreasonable preferences to persons, corporations, or localities; to inhibit greater compensation for a shorter and for a longer distance over the same line; and to abolish combinations for the pooling of freights."

The ill to be cured was economic in nature; those to be protected are those in the shipping field.

### **3. HURNBLAD PRESENTS NOTHING TO SHOW A PROXIMATE CAUSAL CONNECTION BETWEEN THE ALLEGED VIOLATION AND THE INJURY**

Hurnblad takes a full page of his brief (Ans. Br. pp. 18-19) to work up to the rule that there must be a proximate causal relationship between a statutory violation and injury before liability will attach. This basic tort principle is set forth by Foster at pp. 57-58. Using this elementary conclusion as a springboard, Hurnblad then makes the speculative leap to the conclusion that if the proper rate had been charged the accident would not have occurred. He argues that if the proper rate were paid that it would follow as a certainty that the equipment would have been adequately and safely maintained.<sup>7</sup> This is nonsense. Hurnblad forgets that the carrier is free to do with the income as he pleases. The payment of the proper tariff by the shipper is no guarantee that the carrier will not use it to play the stock market or buy

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<sup>7</sup>For all intents and purposes this was the same argument made to the court in *Barsh v. Mullins*, 338 P.2d 845 (Okla. 1959). See pp. 64-65 of App. Br. for the unsympathetic response this argument elicited from the court.

diamond bracelets rather than safety. The proximate cause of the accident was the failure of the driver to either check his brakes or to properly adjust them during the trip. In any event, it is clear that the accident occurred, not because Foster engaged an un-certified carrier, Transport Supply, but because the driver of the truck hired by Transport Supply failed to check his brakes.

### **III. REPLY TO HURNBLAD'S ANSWERING ARGUMENT**

#### **A. A PARTY INJURED BY THE NEGLIGENCE OF AN INDEPENDENT CONTRACTOR WHO HAD A CONTRACT WITH ANOTHER INDEPENDENT CONTRACTOR, WHO HAD A PREVIOUS CONTRACT WITH A THIRD INDEPENDENT CONTRACTOR, HAS NO CLAIM AGAINST THE THIRD INDEPENDENT CONTRACTOR FOR THE NEGLIGENCE OF THE FIRST INDEPENDENT CONTRACTOR**

Hurnblad attempts to show that this issue is not procedurally before this court. All that need be said in this regard is that the independent contractor status of Knight was brought to the trial court's attention in Foster's requested instruction No. 11 (R. 48) which was refused. This was preserved for appeal by Foster on page 919 of the Transcript and included as Specification of Error No. 7 (App. Br. p. 15). This particular question was also brought to the trial court's attention by Hurnblad himself. In his requested instruction No. 27 (R. 90) he inferred that Knight, not Transport Supply, was the independent contractor of Foster. However, the court refused this erroneous construction and gave a correct

charge, stating that Transport Supply was the independent contractor of Foster (R. 164 and 180). To this Hurnblad took exception (911) but did not assign it as error.

Turning to the merits, Hurnblad then argues in succession that Knight was not an independent contractor and even if he were, it is of no moment. On the first point Hurnblad chooses to ignore the case law on this question. The definitive case, cited by Foster at page 31 of Appellant's Brief, which Hurnblad refused to discuss or even acknowledge is *Hollingbery v. Dunn*, 68 Wash.2d 75, 411 P.2d 431 (1966). This case lays out the criteria by which the question of independent contractor is to be resolved, and it directs conclusively that Knight was an independent contractor of Transport Supply.

Hurnblad next contends that even if Knight were an independent contractor to Transport Supply, it would not change the situation since "a franchised carrier may not delegate its duties to an independent contractor." For the first twenty pages of his brief, Hurnblad has maintained that Transport Supply was not franchised.<sup>8</sup> Now Hurnblad attempts to reverse his field, and contends that even if Transport Supply was not franchised, it should have the detriments of a franchised carrier, but none of the benefits. This argument groans under the weight of its own hypocrisy. The California case cited by Hurnblad merely restates the common law rule that one who does in fact hold a franchise from the state cannot delegate the liabilities concomitant with it. Hurnblad's

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<sup>8</sup>Hurnblad even went so far as to accuse Foster of bad faith for allegedly insinuating that it might not have been proven that Transport Supply had no certificate.

argument along this line does not even measure up to a good make-weight argument.

Hurnblad sums up by stating that Foster's employees "accepted Sim Knight's truck by supervising the loading operation". (Ans. Br. 21) And from this he concludes:

"Appellant's negligence, in part, is predicated upon that direct sanction of defendant, Sim Knight, and the use of his unsafe truck to haul appellant's goods." (Ans. Br. 22)

This is patently erroneous, this theory was never submitted to the jury. Foster was never charged with negligently engaging Sim Knight. The only issue submitted to the jury on negilgent engagement of an independent contractor referred to the engagement of Transport Supply Company. (R. 164 and 180)

The net result is that Hurnblad has failed to present any argument to refute Foster's argument that the negligent acts of Knight which caused the harm were too remote in time, space and contractual relationship from Foster to result in any liability to Foster.

#### **B. THE EVIDENCE FAILED TO ESTABLISH ANY NEGLIGENCE IN FOSTER'S CONTRACTING WITH TRANSPORT SUPPLY**

*Come forward with just one example of antecedent incompetency on the part of Transport Supply.* This was the flat challenge laid down by Foster in his opening brief, pp. 41-43. How did Hurnblad reply? Did he point triumphantly to one miniscule piece of evidence overlooked by Foster? No, he did not. Why?

Because he could not. Rather, he dredged the transcript for any reference to the incompetency of Knight (See ft. 2 *supra*, and Argument *supra* p. 9). But the question was: Did Foster negligently select Transport Supply as an independent contractor? (R. 164 & 180). Hurnblad never addressed himself to the question.

Hurnblad presents his answer to Foster's twelve-page argument on this issue in just one page. But in that one page he manages to engage in the irrelevancies of illegal rates, interject emotional phrases such as "'fly-by-night' motor carriers," and ignore completely the Washington cases on this issue. It is this last characteristic which is most disconcerting. Foster set forth in his brief (pp. 34-38) and in this brief (p. 9) the line of Washington cases which come to grips with this issue. However, Hurnblad does not even attempt to meet and argue them. Appellant demanded that Hurnblad show one instance of antecedent incompetence as required by the Washington rule, but Hurnblad ignores this and asks for relief, his burden of proof notwithstanding. The review of Hurnblad's case presented in Appellant's Brief at pp. 41-43 shows clearly that Hurnblad did not introduce one witness who could testify as to any instance of incompetence by Transport Supply.<sup>9</sup>

<sup>9</sup>Hurnblad's attempts to distinguish the cases of *Moore v. Roberts*, 93 S.W.2d 236 (Tex. Civ. App. 1936) and *Mooney v. Stainless, Inc.*, 338 F.2d 127 (6th Cir. 1964) are so transparent they require little answer. Suffice to say that in *Moore* liability was attempted to be imposed on a shipper who sent goods via an independent contractor who did not have a certificate, who used an uncertified driver, and whose bad brakes caused the accident. It would be hard to find a case more clearly on all fours on all relevant facts. *Mooney* involved a plaintiff who was thrown out because she failed, like Hurnblad, to produce any evidence of any antecedent negligence or incompetency on the part of the independent contractor. Both cases are discussed at length in App. Br. pp. 38-41 and 45.

### C. THE EVIDENCE FAILED TO ESTABLISH ANY NEGLIGENCE BY FOSTER REGARDING SECTION 322(c) WHICH WAS A PROXIMATE CAUSE OF PLAINTIFF'S INJURY

Hurnblad makes the remark that neither common sense nor case law support the proposition that the prime body responsible for enforcing the Interstate Commerce Act is the I.C.C. (Ans. Br. p. 23). The inference from this argument is that the duty to enforce the Act falls on the shipper, Foster; that it has a duty to ascertain that the truck driver is properly licensed, that he complies with the health requirements of the I.C.C., that his vision meets the I.C.C. minimums, that the numerous brakes and brake drums on the tractor-trailer rig comply with the detailed I.C.C. regulations, that all the equipment on the truck complies with the detailed I.C.C. regulations (which regulations run to 78 pages, Ex. 9, which was used in part in the instructions R. 157-158), that numbers, if any, on the truck are real numbers issued by the I.C.C., that any permit has not expired, that the haul in question is within the tariffs filed with the I.C.C. (which tariffs sometimes run to hundreds of pages and thousands of rates (35)). All of this and more, according to the appellee, devolves upon Foster as a shipper, and if to Foster, then to every shipper, including the housewife shipping household goods from San Leandro, California to Bellevue, Washington.

Hurnblad's concept of common sense and case law notwithstanding, 49 U.S.C.A. §43 provides:

"Whenever the Interstate Commerce Commission shall have reasonable ground for belief that any common carrier is engaged in the carriage

. . . of freight traffic between given points at less than the published rates on file, or is committing any discriminations forbidden by law, a petition may be presented alleging such facts to the District Court of the United States sitting in equity having jurisdiction. . . ."

Hurnblad then goes on for some three pages about what might have been. He in no way acknowledges that his burden under §322(c) was not to prove "what might have been," but to prove what did in fact occur. As set forth in Foster's Br. pp. 46-51, the burden placed on Hurnblad was (1) to prove that Foster knew that Knight had no certificate *AND* (2) to prove that Foster knew that Transport Supply was charging less than the minimum rate. Under the regime of I.C.C. competition in this regulated sector of the economy is now conducted mainly in areas of service, availability and equipment. Price cutting and discriminations are no longer significant factors which a *shipper* must consider. Hurnblad also talks about the invoice which reflected Transport Supply's below minimum rates. Nowhere in his argument does he own up to the fact that none of the invoices were even received by Foster, prior to the shipment in question. (This was shown in detail at App. Br. p. 50). Hurnblad's contention is premised on retroactive notice which is not the law.

Hurnblad devotes only a four line footnote (Ans. Br. p. 25 ft. 16) to his argument that Foster knew that Knight had no certificate. This is ironically symbolic since on the scale of events this de-minimis reference corresponds to the amount of contact which Foster had with Knight. Knight pulled into the yard, was loaded, and was on his way. What

else transpired at this brief encounter was not shown by Hurnblad. He can only sit and speculate as to what might have been. However, what might have been is not evidence, and without evidence Hurnblad cannot proceed.

Thus, in answer to Foster's two-pronged argument of no showing of knowledge, Hurnblad discusses invoices and what might have been in answer to one prong, and presents absolutely no argument whatsoever to refute the other prong.

This would be an appropriate point for Hurnblad to answer Foster's argument that the statute is inapplicable to Hurnblad (App. Br. pp. 51-57). However, Hurnblad chooses to eschew any reference to the United States Supreme Court cases which have held consistently over a 75 year period that the injury to be prevented is economic not personal, and the groups to be protected are those directly injured by price wars, rebates, discriminations, and extortions. (See *New York v. United States*, 331 U.S. 284 (1947); App. Br. pp. 51-57; App. R. Br. pp. 11-12).

On page 27 of his brief, Hurnblad finally turns and faces two of the many cases which directly contradict his proffered legal theories. However, rather than meet and argue their basic rationale, he attempts to distinguish them. These cases<sup>10</sup> were cited by Foster because they involve attempts by third parties to hold a shipper liable for the negligence of an uncertified motor carrier. In both cases the court held as a matter of law there could be no causal connection between shipping on an uncertified carrier and any

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<sup>10</sup> *Marion Machine, Foundry & Supply v. Duncan*, 187 Okla. 160, 101 P.2d 813 (1949); *Barsh v. Mullins*, 338 P.2d 845 (Okla. 1959). See App. Br. pp. 63-65 for an examination of these cases.

injury which the carrier's negligence might produce. Hurnblad attempts to distinguish these cases on the extraneous grounds that they allegedly did not involve a below the minimum tariff rate and that Oklahoma does not hold a principal liable for negligent selection of an independent contractor. As for the former, the obvious reason that no mention of the tariff was made was that it was absolutely irrelevant on the issue of proximate cause. It is just as irrelevant here, but Hurnblad continues to wave his flag. The second ground for distinction is completely specious. In the first place, the language of the court quoted by Hurnblad shows no more than that the issue has not been presented to the court. It is an old tradition of common law, albeit not always followed, that a court wait for the question to come to it before it gives an answer. But even if that were not the situation, the cases are still valid for the proposition for which they were cited because the question of negligent selection of an independent contractor is irrelevant to this issue.<sup>11</sup>

At this point in his brief (p. 28) Hurnblad makes a most groundless charge. In the middle of his attempts to rationalize the jury's finding of proximate cause, he interjects the completely erroneous and extraneous allegation that Foster is contending that a principal is not liable for negligent selection of an independent contractor. The entire matter of liability resulting from the employment of an incom-

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<sup>11</sup>Hurnblad also attempts to discredit *DeBord v. Proctor & Gamble Distrib. Co.*, 146 F.2d 54 (5th Cir. 1944) by alleging that the 5th Circuit there found the Oklahoma case of *Marion Machine* to be controlling. The 5th Circuit cited *Marion Machine* for the same reason Foster cited *DeBord*: the inherent basic rationale that there is no proximate causal relationship such that a shipper can be held liable for the negligence of an uncertified carrier. For a discussion of *DeBord* see App. Br. p. 59.

petent independent contractor was discussed *supra* at pp. 4-9; 15-16 and in App. Br. at pp. 33-45. Hurnblad's injection of this issue out of order indicates confusion on his part. (See App. Br. pp. 69-74).

Hurnblad concludes his argument on proximate cause with the statement that this case "is not akin to driving a car without a license."<sup>12</sup> He then goes on to draw the truly remarkable conclusion that if Transport Supply had been licensed, then the accident "for certain" would not have occurred.

As indicated in Foster's brief, there are no Washington cases on the precise question of proximate cause where a shipper has shipped on an unlicensed carrier. However, there are a number of Federal Court decisions<sup>13</sup> and state court decisions<sup>14</sup> which considered this precise issue. Five different courts in seven decisions came to the same conclusion: there is no proximate causal relationship between a shipper shipping on an uncertified carrier and any injury resulting from the negligence of the carrier. Hurnblad does not cite one case to the contrary.

<sup>12</sup>Compare this with Hurnblad's statement on page 18, where he explains this whole issue in terms of driving a car without a license.

<sup>13</sup>*DeBord v. Proctor & Gamble Distrib. Co.*, 146 F.2d 54 (5th Cir. 1944); *Kenosha Auto Transp. Corp. v. Lowe Seed Co.*, 362 F.2d 765 (7th Cir. 1966); and *Hoover v. Allen*, 241 F. Supp. 213 (S.D.N.Y. 1965). These are discussed in Foster's Brief at pp. 59-62.

<sup>14</sup>*Bradley v. Chickashaw Cotton Oil Co.*, 184 Okla. 51, 84 P.2d 629 (1938); *Marion Machine, Foundry & Supply v. Duncan*, 187 Okla. 160, 101 P.2d 813 (1940); *Barsh v. Mullins*, 338 P.2d 845 (Okla. 1959). These were discussed at pp. 62-65 App. Br. Another case which reached this same conclusion was: *Newsome v. Dunn*, 103 Ga. App. 656, 120 S.E.2d 205 (1961). See also *Moore v. Roberts*, *supra*, ft. 9 and *Galentine v. Borglum*, 150 S.W.2d 1088 (Mo. App. 1941).

## D. THE RIGHT TO A NEW TRIAL BECAUSE OF SPECIFIC PREJUDICIAL RULINGS

Hurnblad is able to cite only one case in support of his contention that the statute in question can be violated by negligence. This is the case of *United States v. Gunn*, 97 F. Supp. 476 (W.D. Ark. 1950). A careful reading of the opinion by the District Court Judge reveals that he simply ignored the plain meaning of the words "knowingly and willfully" and emasculated their effect in the statute. From the case it appears that all the United States did prove was negligent violation of Section 322 (a). However, the judge's attitude and designs were revealed when he stated (p. 480):

"To permit the defendant to escape punishment would be against the policy of the law."

It is submitted that the cited case was wrongly decided and is authority for nothing. In addition, it should be noted that the case is not followed by any other court, but quite the contrary, the Federal Courts are unanimous in their conclusion that the statute cannot be violated by negligence. In addition to the cases cited in Appellant's Brief,<sup>15</sup> two cases cited by Hurnblad (Ans. Br. p. 24), also state the rule that this statute cannot be violated by mere negligence.<sup>16</sup>

The most fundamental error committed by the trial court was in its instruction on proximate cause (App. Br. pp. 74-76). The "but for" instruction given by

<sup>15</sup>*Inland Freight Lines v. United States*, 191 F.2d 313 (10th Cir. 1951); *United States v. Joralemon Bros., Inc.* 174 F. Supp. 262 (E.D.N.Y. 1959). These appear on pages 68-69 of Appellant's Brief.

<sup>16</sup>*Steere Tank Lines, Inc. v. United States*, 330 F.2d 719 at 721 (5th Cir. 1963); *United States v. E. Brooke Matlack, Inc.*, 149 F. Supp. 814 at 820 (D.Md. 1957).

the court threw off the jury's consideration of both issues here involved. The question presented to the jury by this instruction was: If Foster had not employed Transport Supply would the accident have still occurred? To which the obviously simple answer was no: if Foster had not employed Transport Supply, then Transport Supply would not have employed Knight who would not have been on the road.

Hurnblad can announce only his bare conclusion that the instruction was correct. He makes no attempt to rationalize the court's instruction in light of the Washington case cited<sup>17</sup> which states in clear unequivocal language that an instruction on proximate cause which defines proximate cause under the "but for" concept does not state the Washington rule. Hurnblad attempts to characterize the *Meher* case as concerned with superseding negligence, but a reading of the quotation set forth on page 75 of Foster's brief reveals that the object of discussion was the difference between actual cause and proximate cause. It is clear that the court gave a faulty definition for the ultimate question. No verdict can stand when premised upon such a grossly inaccurate statement of the applicable law.

Foster raised four other trial errors. Two of these, admission of evidence of what a certified carrier would look for,<sup>18</sup> and the charge which made motor carrier safety statutes and regulations applicable to a shipper,<sup>19</sup> were not answered by Hurnblad and

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<sup>17</sup>*Meher v. Easterling*, \_\_\_\_ Wash.2d \_\_\_\_, 71 Wash. Dec. 2d 102, 426 P.2d 843 (1967).

<sup>18</sup>App. Br. p. 73

<sup>19</sup>App. Br. p. 74

they stand unchallenged as evidence of the necessity of a new trial.

The remaining two errors, the admission of Mr. Landsburg's bloody reputation of uncertified carriers,<sup>20</sup> and the repetitive admission of evidence as to illegal rates,<sup>21</sup> were mentioned by Hurnblad, but were not answered. Hurnblad attempts to argue that Mr. Landsburg said no more than Mr. Baker. But Mr. Baker did not create the impression that Foster and Transport Supply got together for an illegal deal in which they cared not how many battered and broken bodies might be strewn along the highway; he did not tell the jury here is your chance to help the I.C.C. with a problem by laying liability to this shipper. Baker said none of these things, but Landsburg did. And, because of the admission of this irrelevant testimony Foster suffered grievous prejudicial harm. Hurnblad still contends that the testimony was not offered to show that any of the parties at trial was a bad guy. The fact that this was the way it came out when Hurnblad introduced it notwithstanding, Hurnblad made no effort, nor did the court, to instruct the jury that Mr. Landsburg was only testifying about what Foster should know, not what this former government official felt Foster actually did do. The singular impression which the jury could draw from this testimony was that here was real proof that Transport Supply and Foster were in an illegal deal together and we should get them for it.

Hurnblad completely skirts the issue raised on the admission of repetitive testimony of illegal rates. He

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<sup>20</sup>App. Br. pp. 69-72

<sup>21</sup>App. Br. pp. 72-73

discusses all the other reasons he had for introducing the testimony of Mr. Connor and Mr. Stewart, but at no point does he answer why during the course of the trial he asked on ten different occasions whether the rate charged by Transport Supply was legal. He does not tell why he kept hammering, hammering and hammering away on the fact that Transport Supply did not charge the legal minimum. The reason he does not tell is because this was the manifestation of his confusion tactic. The only purpose for going over and over and over the same ground was to magnify this aspect to such an extent that the jury would be swept along in the confusion.

## CONCLUSION

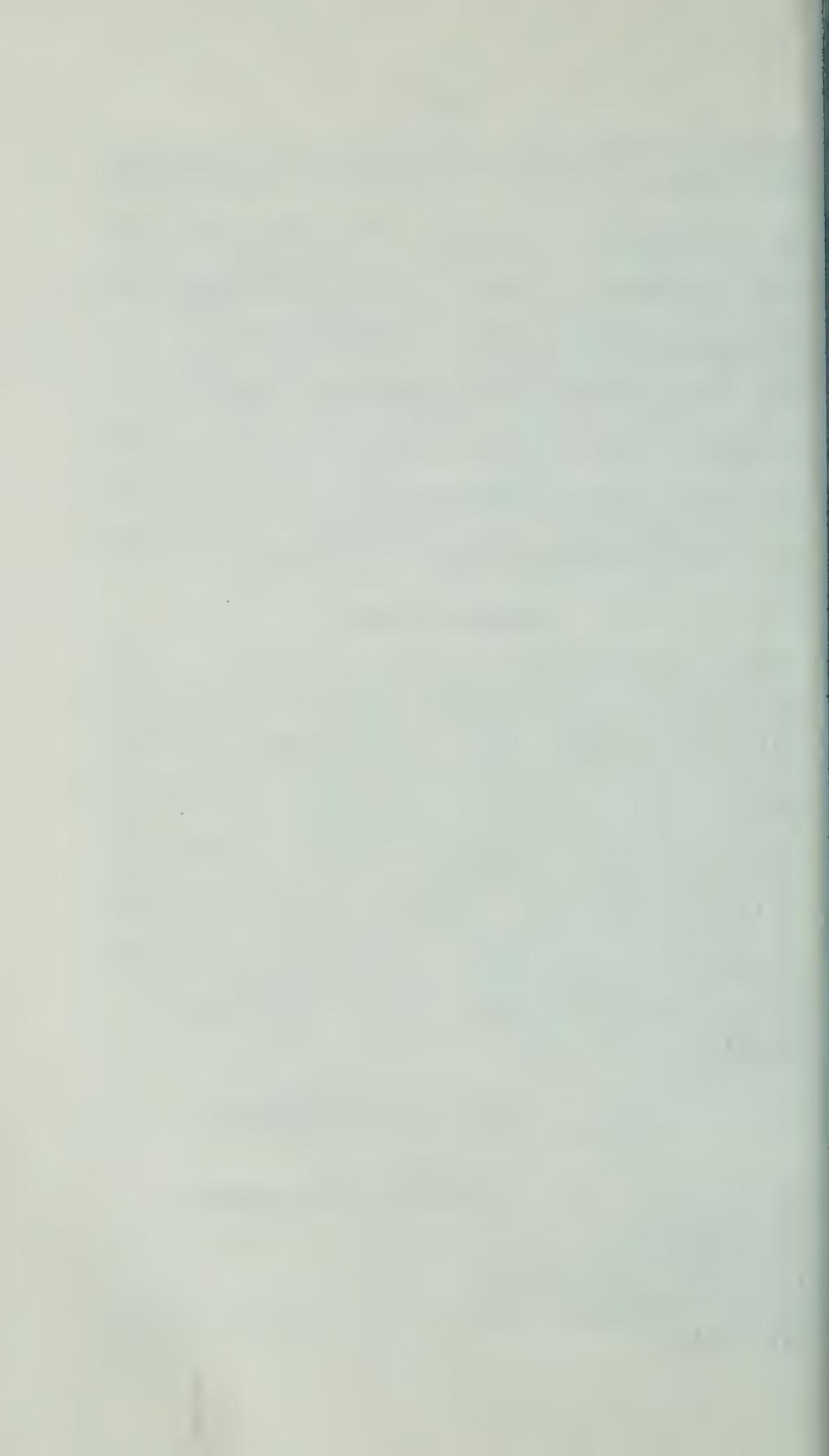
Hurnblad has failed to properly answer any of the arguments or cases raised by Foster. Because of the errors of the trial court on the matters of admissibility and the charge to the jury, the judgment below must be reversed. Because of Hurnblad's failure to carry his burden of proof, his first theory must be stricken, and the judgment below based thereon reversed. Because of Hurnblad's failure to sustain his burden of proof and his failure to show applicability of the statute, his second theory must be stricken and the judgment below based thereon, reversed.

Respectfully submitted,

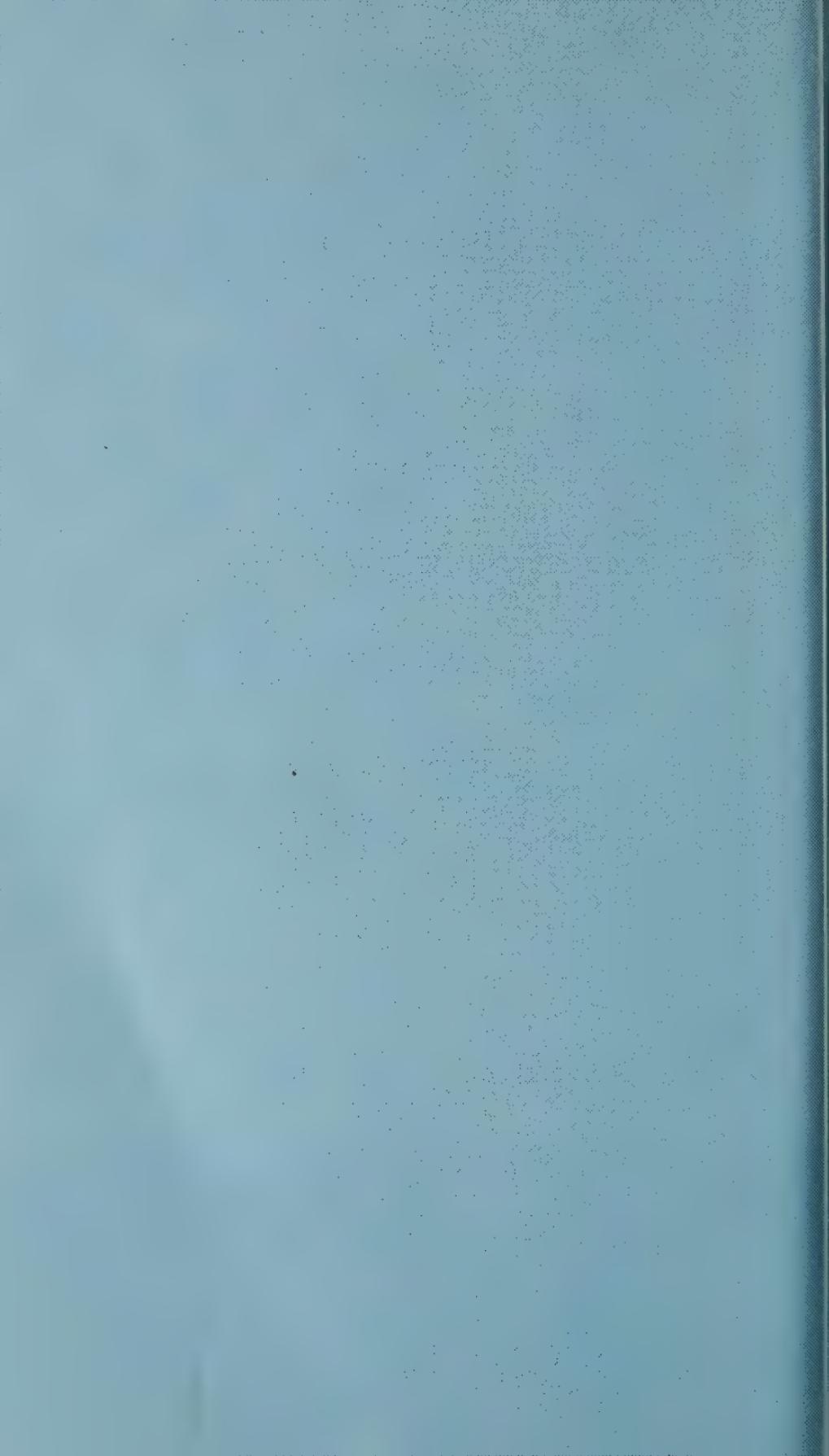
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## **Appendices**



**PREAMBLE TO THE 1940 AMENDMENT TO  
THE INTERSTATE COMMERCE ACT**

“It is hereby declared to be the national transportation policy of the Congress to provide for fair and impartial regulation of all modes of transportation subject to the provisions of this Act, so administered as to recognize and preserve the inherent advantages of each; to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation and among the several carriers; to encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices; to cooperate with the several States and the duly authorized officials thereof; and to encourage fair wages and equitable working conditions; — all to the end of developing, coordinating, and preserving a national transportation system by water, highway, and rail, as well as other means, adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense. All of the provisions of this Act shall be administered and enforced with a view to carrying out the above declaration of policy.”



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In the  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

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No. 22598

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REPUBLIC NATIONAL LIFE INSURANCE COMPANY,  
*Appellant,*  
*v.*

HAMILTON LIFE INSURANCE COMPANY OF NEW YORK and  
FINANCIAL SECURITY LIFE INSURANCE COMPANY,  
*Appellees.*

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**BRIEF OF APPELLANT**

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In the  
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*Appellant,*  
*v.*

**HAMILTON LIFE INSURANCE COMPANY OF NEW YORK and**  
**FINANCIAL SECURITY LIFE INSURANCE COMPANY,**  
*Appellees.*

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**BRIEF OF APPELLANT**

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**JURISDICTION**

The District Court had jurisdiction of this case under 28 U.S.C., Section 1332 as the action was commenced by Appellant, a Texas corporation against Appellee, Hamilton Life Insurance Company of New York, a New York corporation, and Financial Security Life Insurance Company, an Arizona corporation, and involves more than \$10,000. Venue rests in the United States District Court for the District of Arizona, being the District where Financial Se-

curity is incorporated and where Appellant and Appellee are licensed to do business. The action is one for the declaration of the rights and legal relations between the parties arising out of an agreement for reinsurance and coinsurance of insurance business and for the rescission of such agreement, and for such other relief as may be granted. 28 U.S.C., Sections 2201 and 2202.

The United States Court of Appeals for the Ninth Circuit has jurisdiction of this appeal of an order staying a civil action pursuant to the United States Arbitration Act. *Ross v. 20th Century-Fox Film Corp.*, 236 F. 2d 632 (9th Cir. 1956) and *Ets-Hokin and Galvan Inc. v. United States ex rel. Pratt*, 350 F. 2d 871 (C.A. 9, 1965). 28 U.S.C., Sections 1291 and 1292.

### **STATEMENT OF FACTS**

The action now pending appeal was commenced in the United States District Court for the District of Arizona on November 3, 1967, by the Plaintiff, a Texas insurance corporation, against two other insurers, Hamilton Life Insurance Company of New York, a New York insurance corporation (referred to below as "Hamilton") and Financial Security Life Insurance Company, an Arizona insurance corporation (referred to below as "Financial Security") for rescission, damages and a declaratory judgment of the rights and liabilities of the three parties. (Record 1-7) The relationship of the parties arises from a parol reinsurance and coinsurance contract by which certain insurance business originated by the Defendant, Hamilton, was to be ceded for

reinsurance to the Plaintiff, Republic National, upon condition that 80 percent of such insurance be retroceded for further reinsurance by Financial Security. (Record 2-3, 63, 69) Pursuant to this parol contract, the cessions were made as evidenced by two written reinsurance agreements, one between Hamilton and Republic National, and the other between Republic National and Financial Security, both attached to the Complaint. (Record 1-9 and exhibits)

On December 15, 1967, subsequent to the institution of this action, the Plaintiff was served with notice that Hamilton, a defendant in this action, had commenced action under 9 U.S.C. Section 4 on December 11, 1967, in the United States District Court for the Southern District of New York, to compel arbitration of disputes existing between Hamilton and Republic National under the written portion of the reinsurance and coinsurance contract described in Republic National's Complaint. (Record 27) On December 15, 1967, Hamilton filed its Motion for Stay or Proceedings Pending Arbitration pursuant to 9 U.S.C. Section 3, in the United States District Court in Arizona. (Record 10) To prevent the conflicting exercise of jurisdiction, the Arizona District Court temporarily restrained the Defendant, Hamilton, from proceeding in New York (Record 37) and after a hearing, issued an interlocutory injunction to the same effect. (Record 72) Hamilton moved to quash the interlocutory injunction. (Record 75)

Defendant, Financial Security, filed a motion to dismiss for failure to include an indispensable party which was not ruled on by the District Court; Hamilton's motions to sever and dismiss were denied. (These instruments not made part of the record) Appellant filed its Motion for Partial Summary Judgment (Record 63) which was not ruled upon by the Court.

Finally, by its orders of January 29, 1968, (Record 83) and February 15, 1968, (Record 101) the District Court in Arizona granted Hamilton's motion to stay the proceedings in Arizona pending arbitration pursuant to Section 3 of the Federal Arbitration Act, 9 U.S.C. Sections 1-14, while refusing the rule upon Republic National's contention that 15 U.S.C. Sections 1011-1015, commonly called the McCarran Act, exempts the insurance business from the coverage of the Arbitration Act. The injunction against proceedings in New York was then dissolved. (Record 84) The District Court, recognizing the gravity of the legal issues then stayed its own orders until February 26, 1968, (Record 102) to enable Appellant to obtain a continuation of the stay order from the United States Court of Appeals. The District Court orders were temporarily stayed until March 4, 1968, by this Court in its order of February 20, 1968. The temporary stay order was vacated on March 4, 1968.

Republic National filed its notice of appeal to the United States Court of Appeals for the Ninth Circuit (Record 103) and its appeal bond (Record 104).

## **CONTESTED ISSUES**

### **I.**

**Whether the District Court erred in granting a stay under Section 3 of the United States Arbitration Act (9 U.S.C. Section 3) without passing upon the question of whether the McCarran-Ferguson Act (15 U.S.C. Section 1011, et seq.) prohibited its application to insurance companies.**

### **II.**

**Whether the District Court erred in failing to pass upon the facts of whether there was a written arbitration agreement between the parties and arbitrable issues.**

### **III.**

**Whether the District Court could grant a stay under its general stay powers in view of the Kerotest doctrine.**

### **IV.**

**Whether it was error to mandate the questions of fact and law essential to a motion for stay under Section 3 of the Arbitration Act, to the court having jurisdiction of an action to compel arbitration under Section 4 of the Act.**

## **SUMMARY OF ARGUMENT**

Republic National contends that since the United States Arbitration Act is not one of the few federal enactments

specified by the McCarran Act to apply to the business of insurance, and, since the Arbitration Act itself has never specified by its provisions that it specifically applies to insurance companies, the Congressional intent embodied in the McCarran Act (15 U.S.C., Sections 1011-1015) must be obeyed and thus exempts this action from the provisions of the United States Arbitration Act. By contrast, the District Court has read 9 U.S.C., Sections 3 and 4 to require that a stay for arbitration be granted before it is decided if the McCarran Act bars application to these parties of the very act pursuant to which the stay was granted. Republic National submits that it is altogether illogical to obtain any result under the Arbitration Act until it is first established that the subject matter of the contract of reinsurance is within the definition of Sections 1 and 2 of the Arbitration Act.

In addition to this basic jurisdictional question, Republic National submits that even if the United States Arbitration Act applies to the business of insurance, it must first be established that a written arbitration agreement exists among the parties to this dispute and that there are disputed issues in the pending action which are subject to arbitration under the terms of such an agreement, if any. Tri-partite contractual arrangements and issues cannot be hauled into arbitration by the vehicle of a biparte arbitration agreement. These issues must be decided by the court having jurisdiction of the motion for stay and cannot properly be mandated to another district court for decision.

Therefore, because of the failure to pass upon the threshold jurisdictional question resulting from the conflict between the McCarran-Ferguson Act and the United States Arbitration Act, as well as the refusal to pass upon the factual contentions concerning the reinsurance arrangement at issue and the disputes which have arisen under it, the stay order of the district court was granted in error.

In addition, it would have been improper for the court to act under any general stay power inherent in the district courts because of the Kerotest doctrine, which holds that in a concurrent jurisdictional matter the first court to have jurisdiction of the parties and subject matter is the proper court to try the issues. No general stay would be proper and there is nothing in the United States Arbitration Act or any other statute which authorizes the procedures used here of "consolidating" the motion for stay in the Arizona court with the petition to compel arbitration in the New York court.

### **POINT I**

**The Honorable District Court erred in applying Section 3 of the Federal Arbitration Act, as such Act does not apply to insurance companies in view of the McCarran-Ferguson Act (15 U.S.C., Sections 1011, et seq.).**

### **ARGUMENT UNDER POINT I**

The first crucial point to be determined before deciding the question of a stay of action under the United States Arbitration Act is whether the Act itself applies to the con-

tract in question. A stay under Section 3 of the Act can only be granted when contracts subject to Sections 1 and 2 are involved. *Bernhardt v. Polygraphic Company of America*, 350 U.S. 198, 76 S. Ct. 273 (1956), *Ross v. Twentieth Century-Fox Film Corp.*, 236 F. 2d 632 (9th Cir. 1956), *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 87 S. Ct. 1801, ..... L. Ed. ..... (1967). The Honorable District Court's refusal to rule on this threshold issue, while at the same time granting a stay under Section 3, is basic error. The application of the Arbitration Act to a contract outside the scope of Sections 1 and 2 of the Arbitration Act invades the province of local law reserved to the states by *Erie Railroad v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, and *Bernhardt*, *supra*.

The Federal Arbitration Act applies to a contract evidencing transactions involving commerce, containing written arbitration provisions. 9 U.S.C., Section 2. The Act derives its authority from Article 1, Section 8, Clause 3 of the United States Constitution, which gives to Congress the power to regulate commerce among the several states. It is the Appellant's position that the United States Arbitration Act does not apply to insurance companies because of the McCarran-Ferguson Act. The Arbitration Act does not apply to all matters and has not been applied when in conflict with more specific acts which are definitive of public policy. See *Wilco v. Swan*, 346 U.S. 427, 64 S. Ct. 182, 98 L. Ed. 168 (1954) and *American Safety Equipment Co. v. J. P. McGuire & Co.*, ..... F. 2d ..... (2d

Cir Mar. 20, 1968). The history of the McCarran Act is important to this issue.

In 1944 the Supreme Court, in *United States v. South-Eastern Underwriters Association*, 322 U.S. 533, 64 S. Ct. 1162, held that the business of insurance was interstate commerce. It has been held that reinsurance is the business of insurance. *Connecticut General Life Insurance Co. v. Johnson*, 303 U.S. 77, 58 S. Ct. 436 (1938). Following the turmoil created by the South-Eastern decision, Congress passed in 1945 the McCarran-Ferguson Act, widely known as Public Law 15 and contained at 15 U.S.C., Sections 1011-1015. This statute, with certain exceptions, left to the states the regulation of the business of insurance. The declaration of Congressional policy is contained in the first section of the Act, 15 U.S.C., Section 1011, as follows:

“Congress declares that the continued regulation and taxation by the several states of the business of insurance is in the public interest, and that silence on the part of Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several states.”

Section 1012 provides:

“(b) No act of Congress shall be construed to invalidate, impair or supersede any law enacted by any state for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business unless such act specifically relates to the business of insurance:  
\* \* \*”

The proviso stated that after a moratorium which would be in existence until June 30, 1948, the Clayton Act, the Federal Trade Commission Act and the Sherman-Antitrust Act

would not apply to the business of insurance to the extent the business was regulated by the state law. Section 1014 provided exceptions to the broad mandate returning insurance business to state control by specifically making the insurance business subject to certain Federal acts. These included the National Labor Relations Act, the Fair Labor Standards Act and the Merchant Marine Act.

All decisions construing the scope of the McCarran Act to date have drawn heavily upon the historical context of its enactment. In 1869, the Supreme Court held that issuing a policy of insurance was not a transaction in commerce. *Paul v. Virginia*, 8 Wall. 168-185, 19 L. Ed. 357 (1869). Subsequent cases consistently held that the business of insurance was not commerce. *New York Life Insurance Co. v. Deer Lodge County*, 231 U.S. 495, 503-504, 510, 34 S. Ct. 167, 172, 58 L. Ed. 332 (1913). It was unexpected, therefore, when in 1944 the United States Supreme Court, in *United States v. Southwestern Underwriters Association*, *supra*, held that the business of insurance was interstate commerce, and subject to regulation by Congress under the commerce clause.

In swift reaction to the *South-Eastern Underwriters* case, Congress enacted the McCarran-Ferguson Act in 1945. 15 U.S.C., Sections 1011-1014. An excellent historical narrative is incorporated in the opinion in *National Casualty Co. v. FTC*, 245 F. 2d 883, 887 (6th Cir. 1957) aff'd., 357 U.S. 560, 78 S. Ct. 1260 2 L. Ed. 2d 1540 (1958).

The overriding concern embodied in the McCarran Act was to recreate a broad field for state regulation of the insurance industry free from federal intervention, subject

only to certain exceptions specifically embodied in the Act. *National Casualty Co. v. FTC*, supra. In *SEC v. National Securities, Inc.*, 387 F. 2d 25, 29 (9th Cir. 1967) it is stated that the original reaction to *South-Eastern Underwriters* was a desire to exempt insurance from federal antitrust regulation, but that the final enactment stated a far broader policy of exclusion:

“The focus shifted from a narrow exemption from the Sherman and Clayton Acts to a general policy of exemption with specific exceptions to that policy.”

Federal enactments in the interstate commerce field prior to the McCarran Act made no mention of the exemption for insurance companies because the exemption from interstate commerce recognized in *Paul v. Virginia* was so generally accepted that Congress legislated only in terms applicable to commerce generally, without particularized reference to insurance. *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408, 415, 66 S. Ct. 1142, 90 L. Ed. 1342 (1946); *SEC v. National Securities, Inc.*, supra.

It was during this period when the insurance business was considered outside the field of interstate commerce regulation that the Federal Arbitration Act, 9 U.S.C., Sections 1-14, was enacted in 1925. Consequently, prior to *South-Eastern Underwriters* in 1944, the Federal Arbitration Act had no application to the insurance business. During the interim between that decision and the enactment of the McCarran Act, it could be inferred that the Arbitration Act, together with all other federal acts relating to interstate commerce, would be potentially applicable to the business of insurance.

After the *South-Eastern Underwriters* decision, the Federal Arbitration Act was not applied to insurance companies in any reported cases, presumably because the doctrine of *Erie R.R. v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188 (1938) was generally thought to make the substantive outcome of an arbitration case depend upon applicable state laws. This distinction was the controlling consideration in *Bernhardt v. Polygraphic Company of America*, *supra*. It was not until June 1967, with the decision in *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, *supra*, that the concept of federal substantive law embodied in the Arbitration Act distinguished this body of law from the *Erie* doctrine. This evolution explains why in the forty-three years which have intervened from the enactment of the Federal Arbitration Act this is the first known case to consider the resulting conflict between the McCarran Act and the Federal Arbitration Act.

Because of McCarran's historical context and the void of insurance cases under the Arbitration Act, it becomes important to recognize what the courts have held to be the scope of the general McCarran Act exemption. Even though the McCarran Act's genesis was directed toward exempting the insurance business from the Sherman and Clayton Acts, in its final enactment the Act generally excepted the insurance business from all coverage by past, present, and future federal statutes which do not otherwise specifically include the insurance business within their coverage. *SEC v. National Securities, Inc.*, *supra*. So important is this dis-

tinction that the circuit court included in its opinion the following excerpt from the Congressional Record by Senator Ferguson, the co-author of the bill:

"If there is on the books of the United States a legislative act which relates to interstate commerce, if the act does not specifically relate to insurance, it would not apply at the present time. Having passed the bill now before the Senate, if Congress should tomorrow pass a law relating to interstate commerce, and should not specifically apply the law to the business of insurance, it would not be an implied repeal of this bill, and this bill would not be affected, because the Congress had not, under subdivision (b), said that the new law specifically applied to insurance.' 91 Cong. Rec. 481 (1945)."

On the same point, the circuit court also included these statements by Senators Ferguson and O'Mahoney:

"MR. FERGUSON. What we have in mind is that the insurance business, being interstate commerce, if we merely enact a law relating to interstate commerce, or if there is a law now on the statute books relating in some way to interstate commerce, it would not apply to insurance. We wanted to be sure that the Congress, in its wisdom, would act specifically with reference to insurance in enacting the law.

"MR. O'MAHONEY. In other words, no existing law and no future law should, by mere implication, be applied to the business of insurance.

"MR. FERGUSON. That is correct.' 91 Cong. Rec. 1487 (1945)."

Under the scheme of the McCarran Act, this general exemption effected a moratorium on the enforcement of federal statutes in the insurance business, and thereby restored the status quo as it existed prior to *South-Eastern Underwriters. National Casualty Co. v. FTC*, supra. How-

ever, under the provisions of Section 2(b) (15 U.S.C., Section 1012(b)) the moratorium expired on a specified date as to the Sherman Act, Clayton Act and the Federal Trade Commission Act, so that these acts would then become applicable to the insurance industry "to the extent that such business is not regulated by state law." Therefore, in cases involving these three specific federal acts made conditionally effective with regard to insurance under Section 2(b), the courts are continually concerned with first establishing that the state governments have affirmatively acted to regulate within these areas before acknowledging the McCarran Act exemption. Typical of these cases are *FTC v. Travelers Health Association*, 362 U.S. 293, 80 S. Ct. 717, 4 L. Ed. 2d 724 (1960), involving Federal Trade Commission Act; and *United States v. Chicago Title & Trust Co.*, 242 F. Supp. 56 (N.D. Ill. 1965) involving Clayton Act interpretation.

We are here concerned with the broad powers left to the states to regulate the business of insurance. As pointed out in *Prudential Insurance Co. v. Benjamin*, supra, the purpose of the Act was:

"Obviously Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance. This was done in two ways. One was by removing obstructions which might be thought to flow from its own power, whether dormant or exercised, except as otherwise expressly provided in the Act itself or in future legislation. The other was by declaring expressly and affirmatively that continued state regulation and taxation of this business is within the public interest and that the business and all who engage in it 'shall be subject to' the laws of the several states in these respects."

The mandate of the McCarran Act, in common everyday language, allows the states to regulate the business of insurance without any interference or priority by the Federal law except as to specifically designated areas, such as the Labor Relations Act and the Fair Labor Standards Act. But what is meant by the regulation of the insurance business? A state regulates the business of insurance within the meaning of Section 1012(a) and (b), 15 U.S.C., when a state statute generally prescribes or permits or authorizes certain conduct on the part of the insurance companies. If a state has generally authorized or permitted or prohibited certain standards of conduct, it is regulating the business of insurance under the McCarran Act. *California League of Independent Insurance Producers v. Aetna Casualty & Surety Co.*, 175 F. Supp. 857 (N.D. Cal. 1959) citing for authority *FTC v. National Casualty Co.*, 357 U.S. 560, 79 S. Ct. 1260 (1958). "Regulate" means to govern or direct according to rule, or to bring under control of constituted authority, to limit and prohibit, to arrange in proper order, and to control that which already exists. *Farmington River Co. v. Town Plan & Zoning Comm.*, 197 A. 2d 653, 660 (Super. Ct. Conn. 1963). Regulation may be by legislation, as well as by rule. *FTC v. National Casualty*, supra. Regulation prescribes the rule by which something is to be governed. *U. S. v. Darby*, 312 U.S. 100, 113, 61 S. Ct. 451, 456; *Gibbons v. Ogden*, 9 Wheat. 1, 196, 6 L. Ed. 23.

It is not necessary that the regulation contemplated by the McCarran Act be specifically, directly and solely pointed at insurance companies. No state need specifically designate

insurance companies as being within the coverage of its "regulation" in order to constitute regulation within the meaning of Section 2(a) and (b) of the McCarran Act. See *Travelers Health Association v. Virginia*, 339 U.S. 643, 70 S. Ct. 927 (1950), where Virginia's Blue Sky Law enforced by the corporation commission was upheld in its application to insurance companies. In *Professional & Businessmen's Life Insurance Co. v. Bankers Life Insurance Co.*, 163 F. Supp. 274 (D. Mont. 1958), the court concluded that an act generally applicable to all persons and corporations is sufficiently broad to constitute regulation under the McCarran Act concept.

### THE STATE ARBITRATION POLICY

Texas, New York and the majority of other states have dealt with the regulation of insurance in connection with arbitration matters as shown by the passage of various arbitration acts. The Texas arbitration policy is founded on provisions of the Texas Constitution which provides, in Section 13, Article XVI:

"It shall be the duty of the Legislature to pass such laws as may be necessary and proper to decide differences by arbitration, when the parties shall elect that method of trial."

Then, pursuant to the Constitution, the Legislature set forth the then controlling policy of Texas in the original Title 10, Article 224:

"All persons desiring to submit any dispute, controversy or right of action supposed to have accrued to either party, to arbitration, shall have a right to do so in accordance with the provisions of this title."

The public policy of the State of Texas, as expressed in the statute, did not permit the enforcement of contracts to arbitrate future disputes — only existing disputes. 6 Tex. Jur. 2d "Arbitration" Sec. 20, *San Benito C. C. Drain. Dist. v. Farmers State Guar. Bk.*, 192 S.W. 1145 (Civ. App. 1917) writ ref'd., *Tejas Development Co. v. McGough Bros.*, 165 F. 2d 276, 280 (5th Cir. 1947), *Huntington Corp. v. Inwood Construction Co.*, 348 S.W. 2d 442 (Civ. App. 1961) writ ref'd., NRE.

In 1965, this public policy was changed to allow arbitration agreements as to future disputes, specifically excepting, however, insurance matters.

This is consistent with the position stated by Senator McCarran with regard to the scope of the Federal Act:

"It is not required that the assertion of state regulatory authority over a particular phase or practice of the insurance business shall provide the most effective regulation possible or that it shall be equally strict as the applicable Federal law in the same field. Congress has recognized the right of the states to apply their own policy in the regulation of the business of insurance."

Whether the McCarran Act excludes insurance disputes from the Arbitration Act does not rest on the degree of positive regulation exercised by any state. According to *SEC v. National Securities, Inc.*, supra, the fact that the Federal Government has not seen fit specifically to include life insurance under the terms of the Federal Arbitration Act excludes its application to insurance companies. In

*Prudential Insurance Co. v. Benjamin*, supra, the court recognized that uniformity among the states in regulation is not the test.

It can hardly be said that the Federal Arbitration Act would not invalidate, impair or supersede the law of the State of Texas in regard to the precise question of enforceability of arbitration agreements as to future disputes.

While Appellant has placed in the record evidence to show that the contract here involved was a Texas contract, Hamilton has done nothing to produce for the record any evidence contradicting that of the Appellant. Hamilton has made references to its position that the contract is a New York contract, but such references have been contained only in its briefs, and such does not amount to evidence.

It is of small benefit to Hamilton, even ignoring the evidentiary problem, to attempt to impose the status of a New York contract in this case. The New York Arbitration Law holds that when the validity of a contract containing an arbitration clause is at issue it is a matter for determination by the courts and not the arbitrators. Among the exceptions to the enforceability of arbitration contracts under the New York Statute are cases where it is contended the contract is voidable or never came into existence, and contentions of the illegality of the contract, these being questions going to the contract itself, and thus being matters for the court to decide. *Exercycle Corp. v. Maratta*, 9 N.Y. 2d 329, 174 N.E. 2d 463 (N.Y. Ct. App. 1961).

The Honorable District Court chose to grant a stay under Section 3 of the Federal Arbitration Act, although reserving serious doubts as to its application to this case in view of the McCarran Act. The applicability of the McCarran Act to the case at bar posed a basic jurisdictional question to be decided before Section 3 of the Arbitration Act could be determined to be applicable. This jurisdictional question was not decided as required by the Statute and by the Supreme Court cases of *Bernhardt*, *supra*, and *Prima Paint*, *supra*.

## POINT II

**The Honorable Trial Court erred in granting a stay under Section 3 of the Arbitration Act because there was no evidence of any issues involved in the proceeding which were referable to arbitration under an arbitration agreement between the parties.**

### ARGUMENT UNDER POINT II

Section 3 of the Federal Arbitration Act provides as follows:

"If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, *upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement*, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration. July 30, 1947, c. 392, Sec. 1, 61 Stat. 669." (emphasis ours)

Neither of the Defendants in the Trial Court have filed responsive pleadings on the merits to Plaintiff's Complaint. Hamilton filed motions relating to its request for stay under 9 U.S.C., Section 3, claiming that disputes were involved which were properly referable to arbitration under a written arbitration agreement. The proceeding for a stay under the Federal Arbitration Act is considered an application for injunction. *Shanferoke Coal & Supply Corp. v. Westchester Service Corp.*, 293 U.S. 449, 55 S. Ct. 313 (1935). As such the party moving for the stay has the burden of persuasion in showing facts which will authorize a stay under 9 U.S.C., Section 3. It was the first duty of the Honorable District Court, under Section 3 (assuming said Arbitration Act is applicable) to determine whether there was a written agreement to arbitrate and whether any of the issues raised in the suit were within the reach of the agreement.

The leading case to this effect arose in the Second Circuit in *Engineers Association v. Sperry Gyroscope Co.*, 251 F. 2d 133 (2d Cir. 1957). There, the Court of Appeals recognized that the determination of the arbitrability of the grievance depended upon the same facts relevant to a decision by an arbitrator upon the merits of the grievance. The Court held that the fact that the same issues would be involved in both proceedings did not relieve the Trial Court from determining the facts as a prerequisite to adjudging the dispute arbitrable. In emphasizing this point the Court stated:

"This duty cannot be adequately performed unless the court examines the facts upon which the demand for arbitration is based as those facts relate to the language

of the agreement. See *Industrial Trades Union v. Woonsocket Dyeing Co.*, D.C. R.I. 1954, 122 F. Supp. 872. To make out a case for arbitration, Sperry's alleged breach must be 'put into issue by facts, as distinguished from unsupported charges. \* \* \*' Application of Berger, *supra*, 78 N.Y.S. 2d at page 532; *General Olympic Co. v. United Electrical Radio & Machine Workers*, 1949, 300 N.Y. 252, 90 N.E. 2d 181."

It is also the prevailing rule in the Ninth Circuit that the submission to arbitration rests in the first instance on a determination of all relevant fact issues regarding whether the dispute is one subject to arbitration. In *Ets-Hokin & Galvan, Inc. v. United States ex rel. Albert S. Pratt, Inc.*, 350 F. 2d 871 (9th Cir. 1965), upon appeal of the order denying a stay, the Court vacated the order and remanded to the District Court, holding that relevant facts supplied by a record of a state court action must be examined before a competent determination of the arbitration question could be made.

While the pleadings amply demonstrate the terms of two written undertakings between Hamilton and Republic on the one hand, and between Republic National and Financial Security on the other, the substance of Point I in the Complaint is that the entire contract to be construed consisted of parol agreements between all three of the companies, pursuant to which the portions of the agreement relating to certain aspects of the actual cession of life cases were committed to the biparty contracts. This is demonstrated by the affidavit of Mr. William A. Boles.

Mr. Boles states that there were no negotiations for any arbitration agreement between the three parties. Most assuredly, no writing has been produced to date which will conform to the requirement of 9 U.S.C., Section 3.

Also, from the Boles affidavit, it is clear that the entire contractual arrangement was dependent upon a single exchange of consideration, which supports the allegations of the Complaint that the relationship between the three parties for which declaratory judgment is sought was a single integration, which was then reduced to writing as concerns the cession agreements between Republic National and Hamilton, and between Republic National and Financial Security. The record is completely devoid of any evidence submitted by Hamilton denying the existence of arrangements between the three parties to this lawsuit. Instead, Hamilton seeks only to splinter the existing lawsuit into two or more lawsuits by pleading the Federal Arbitration Statute, and by this procedural maneuver seeks to divorce itself from its prior connection and participation in the handling of the reinsurance and coinsurance of this business with its sister company, Financial Security.

As stated in the Statute (9 U.S.C., Section 3) the Court must be "satisfied that the issue involved in such suit \* \* \* if referable to arbitration." As the record stands it is completely devoid of any evidence at all which would show the existence of arbitrable issues involved in the present case. Aside from a legal memorandum claiming that some other district court should decide these issues, Hamilton has not sought to introduce evidence or identify what

arbitrable issues and claims make this case referable to arbitration as provided in Section 3 of the Arbitration Act. Since nothing more was produced, Plaintiff's affidavits on the subject would be controlling and Hamilton's burden of proof has not been met.

If a factual dispute can be demonstrated by Hamilton through materials authorized under Rule 56, then the issues will have been joined and subjected to determination by the proper rules of evidence under the authority of *Engineers Association v. Sperry Gyroscope*, supra. The Federal Arbitration Act can only be invoked upon the foundation of proven fact demonstrating that the Act itself is in fact applicable. This involves not only the jurisdictional questions presented by Republic National but also the factual questions of the existence of a written arbitration agreement between the parties and the further finding of the existence of arbitrable disputes or issues. Since Hamilton wholly failed to carry its burden in establishing such issues and agreement, there was nothing upon which the Trial Court could make findings of fact in support of its order staying a litigation.

### **POINT III**

**Although the District Court's inherent power to stay its own actions is not involved in this case, it would not be properly applicable.**

### **ARGUMENT UNDER POINT III**

Hamilton did not base its motion for stay upon any general power of the Court, although such was referred to in part of its briefing. The motion upon which the orders

were granted was a motion to stay, under 9 U.S.C., Section 3. The Court itself did not invoke any general stay power, basing its order solely and specifically upon Section 3 of the Federal Arbitration Act.

No stay under general powers of courts would have been proper in this case. Plaintiff filed its Complaint in the District Court on November 3, 1967. On November 11, 1967 Hamilton filed a petition to compel arbitration in the Southern District of New York, followed by a motion dated December 15, 1967 in the District Court for the District of Arizona moving for, among other things, a stay of action pending arbitration. The District Court of Arizona had jurisdiction of the subject matter and all the parties prior to the action of Hamilton to compel arbitration in the Southern District of New York or to stay the Arizona proceedings pending arbitration.

The situation presented to the Court by the sequence of events summarized above has been the subject of frequent judicial discussions in the last few years. A typical situation of the kind presented here is one where party A commences an action against party B in one jurisdiction, followed by a suit involving the same issues and parties, together with a third party in another district court. The question which naturally develops is in which of the two courts the proceedings shall be heard to conclusion. If the question is not resolved there could conceivably result two hearings involving the same issues being prosecuted in two different jurisdictions.

The leading case on this point is *Kerotest Manufacturing Co. v. C-O Two Fire Equipment Co.*, 189 F. 2d 31 (3d Cir. 1950). There, the Circuit Court held that the court which first acquired jurisdiction of all the parties necessary to decide all issues and controversies existing between the parties should be the correct forum to retain jurisdiction. In commenting on this, the court said:

"In the instant case the whole of the war and all the parties to it are in the Chicago theatre and there only can it be fought to a finish as the litigations are now cast. On the other hand if the battle is waged in the Delaware arena there is a strong probability that the Chicago suit nonetheless would have to be proceeded with for Acme is not and cannot be made a party to the Delaware litigation. The Chicago suit when adjudicated will bind all the parties in both cases. Why, under the circumstances, should there be two litigations where one will suffice? We can find no adequate reason. We assume, of course, that there will be prompt action in the Chicago theatre."

This case was subsequently affirmed by the U.S. Supreme court, which cited the quoted language of the Third Circuit opinion with approval, and held that the proper remedy was to enjoin the parties from proceeding with the litigation of the parallel case in any other jurisdiction. *Kerotest Manufacturing Co. v. C-O Two Fire Equipment Co.*, 302 U.S. 180, 2 S. Ct. 219 (1952).

Following the *Kerotest* doctrine there has developed an impressive succession of cases from the various circuit courts which are applicable in this situation. In *Martin v. Graybar Electric Co., Inc.*, 255 F. 2d 202 (7th Cir. 1959), the court held that a district court may consider this jurisdictional

question as a matter of discretion, but that discretion must be applied objectively, and if the district court abuses that discretion it may constitute reversible error. In that case, the court applied the following rule relevant to the present action:

"Two simultaneously pending lawsuits involving identical issues and between the same parties, the parties being transposed and each prosecuting the other independently, is certainly anything but conducive to the orderly administration of justice. We believe it to be important that there be a single determination of a controversy between the same litigants and, therefore, a party who first brings an issue into a court of competent jurisdiction should be free from the vexation of concurrent litigation over the same subject matter, and an injunction should issue enjoining the prosecution of the second suit to prevent the economic waste involved in duplicating litigation which would have an adverse effect on the prompt and efficient administration of justice unless unusual circumstances warrant. As none such appears in this record, we agree with what would seem to be the established general rule that the party filing later in time should be enjoined from further prosecution of his suit. (Case citations omitted)"

As a further outgrowth of the *Kerotest* doctrine, the Court of Appeals for the Second Circuit in 1961 held that the first court to obtain jurisdiction over the parties and of all the issues in controversy should proceed with an adjudication of the case on its merits, and that the parties attempting to litigate elsewhere are properly enjoined, stating the rule as follows:

"The bulk of authority supports the position that when a case is brought in one federal district court, and the case so brought embraces essentially the same trans-

actions as those in a case pending in another federal district court, the latter court may enjoin the suitor in the more recently commenced case from taking any further action in the prosecution of that case. (Citations omitted)" *National Equipment Rental, Ltd. v. Fowler*, 287 F. 2d 43 (2d Cir. 1961).

Of particular importance to this case is the decision in *Small v. Wageman* 291 F. 2d 734 (1st Cir. 1961). Here, the same subject matter was before two different district courts, but less than all of the parties to the first action were involved in the subsequent suit. The court observed that the sound judicial policy of avoiding a multiplicity of actions dictates that the court which has jurisdiction of sufficient parties to hear the entire controversy should proceed, and enjoin the parties from litigating the same subject matter in another district. That court pointed out that to do otherwise would conceivably result in two actions in different jurisdictions, neither of which could be completely dispositive of all the questions which could be determined if all of the parties were to be heard in the single jurisdiction which had jurisdiction over all of them.

In the present case, the court for the Arizona District has jurisdiction to determine all questions relating to rights between the three insurance companies under their coinsurance and reinsurance arrangement, and the respective constituent written contracts. It is only in the Arizona District Court that jurisdiction of all the parties lies and it is only there that the full consideration and final determination of the rights, duties, and obligations of all the parties to the coinsurance arrangement can be determined. The District Court fully acknowledged the Kerotest doctrine and

rule in granting the preliminary injunction against Hamilton proceeding in the New York action.

It is for these reasons that no general stay proceedings would have been properly entered by the Arizona Court and the Court correctly did not base its orders upon the application of such power.

#### **POINT IV**

**The Honorable District Court erred in holding that the issues under Section 3 and Section 4 should be considered together in the action pending under Section 4 of the Arbitration Act.**

#### **ARGUMENT UNDER POINT IV**

The Court in its order indicated that defenses to the charge of refusal to arbitrate should be heard and determined in connection with the petition to compel arbitration, which was pending in the United States District Court for the Southern District of New York. The only issue in question in New York is the question raised under 9 U.S.C., Section 4, which provides for the petition for an order to compel arbitration. The Statute provides as follows:

"A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any court of the United States which, save for such agreement, would have jurisdiction under the judicial code at law, in equity, or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. \* \* \* The court shall hear the parties, and upon being satisfied that

the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. \* \* \*

Section 3 of the Arbitration Act provides:

"If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration. July 30, 1947, c. 392, Sec. 1, 61 Stat. 669."

These statutes are not mutual, as envisioned by the Appellee. Apart from the obvious inconsistency of mandating questions to be decided from one district court to another, the Supreme Court has delineated the issues which can be raised under 9 U.S.C., Section 4, and it would be impossible for the New York District Court to consider the issues properly raised under Section 3 as part of the petition under Section 4 without exceeding the limits that the Supreme Court has recognized. In *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 87 S. Ct. 1801, 1806, the court stated:

"Under Section 4, with respect to a matter within the jurisdiction of the Federal Courts save for the existence of an arbitration clause, the court is instructed to order arbitration to proceed once it is satisfied that 'the making of the agreement for arbitration or the failure to

comply (with the arbitration agreement) is not in issue:’”

The existence of arbitrable issues is solely for determination under Section 3, which in turn is dependent upon finding that the act itself is the proper rule of law to be applied to the subject matter at issue.

An action under Section 3 of the Arbitration Act, if successful, merely arrests further action by the court itself in the lawsuit until something outside the suit has occurred. The court does not order that that outside action shall be done. Under Section 4 the court, through the exercise of discretionary equity powers, affirmatively orders that someone do some act outside the suit. The absence of the power to compel performance of an arbitration agreement by the court in which a motion to stay under Section 3 is filed, is not destructive of that court’s jurisdiction. See *Shanferoke Coal & Supply Corp. v. Westchester Service Corp.*, 293 U.S. 449, 55 S. Ct. 313, 79 L. Ed. 583 (1935) and *Kulukundis Shipping Company v. Amtorg Trading Corp.*, 126 F. 2d 978, 988 (2d Cir. 1942). It is, of course, possible that some of the same issues may be involved in the action under Section 4 as would be involved under Section 3, but this is no different than the existence of some identity of issues in two proceedings, one a court and one an arbitration tribunal. In such a case, *Engineers Association v. Sperry Gyroscope Co.*, 251 F. 2d 133 (2d Cir. 1957) the court held that such an identity of issues in the two proceedings would not relieve the court of its duty to determine whether arbitrable disputes existed. What the court has here attempt-

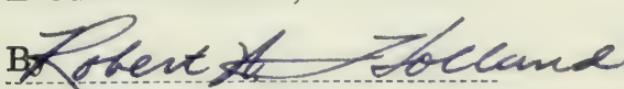
ed is the transfer of the limited questions of jurisdiction and fact to another district court for decision by use of a 9 U.S.C., Section 3 stay. Hamilton filed a motion to sever and transfer all actions against it to New York and such motion was overruled, and properly so. *Hoffman v. Blaski*, 363 U.S. 335, 80 S. Ct. 1084 (1960). There is no authority for the partial "transfer or consolidation" here attempted.

### CONCLUSION

WHEREFORE, for the reasons above discussed, the action of the Honorable District Court in staying its action and referring questions of law and fact to another district court without first passing upon the jurisdictional questions involved, the application of the McCarran-Ferguson Act to the subject matter of this suit, and the failure to find facts necessary under Sections 1, 2 and 3 of the United States Arbitration Act was in error and the orders of the District Court should be reversed.

Respectfully submitted,

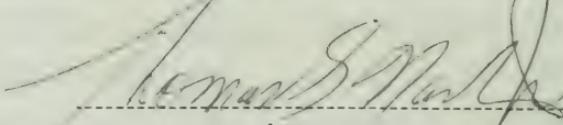
  
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I certify that, in connection with the preparation of this brief I have examined Rules 18, 19, and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing Brief is in full compliance with those rules.



Thomas J. Walsh  
Attorney

A copy of the foregoing Brief has been served by mail this 1st day of May, 1968, upon Mr. John P. Frank of the firm of Lewis, Roca, Beauchamp & Linton, 114 West Adams Street, Phoenix, Arizona 85003, Attorneys for Appellees.



Robert D. Hollan

**UNITED STATES CODE  
ANNOTATED**

**TITLE 9  
ARBITRATION**

Section 1. "Maritime transactions" and "commerce" defined; exceptions to operation of title

"Maritime transactions", as herein defined, means charter parties, bills of lading of water carriers, agreements relating to wharfage, supplies furnished vessels or repairs to vessels, collisions, or any other matters in foreign commerce which, if the subject of controversy, would be embraced within admiralty jurisdiction; "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 2. Validity, irrevocability, and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle

by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 4. Failure to arbitrate under agreement; petition to United States Court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for

arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues

to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof. As amended Sept. 3, 1954, c. 1263, Section 19, 68 Stat. 1233.

**UNITED STATES CODE  
ANNOTATED**

**TITLE 15  
COMMERCE AND TRADE  
SECTIONS 1011-1014  
THE McCARRAN-FERGUSON ACT**

**Section 1011. Declaration of policy**

Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States. Mar. 9, 1945, c. 20, Sec. 1, 59 Stat. 33.

**Section 1012. Regulation by State law, Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948**

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the

business of insurance: Provided, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law. Mar. 9, 1945, c. 20, Secs. 2, 59 Stat. 34; July 25, 1947, c. 326, 61 Stat. 448.

Section 1013. Suspension until June 30, 1948, of application of certain Federal laws; Sherman Anti-Trust Act applicable to agreements to, or acts of, boycott, coercion, or intimidation

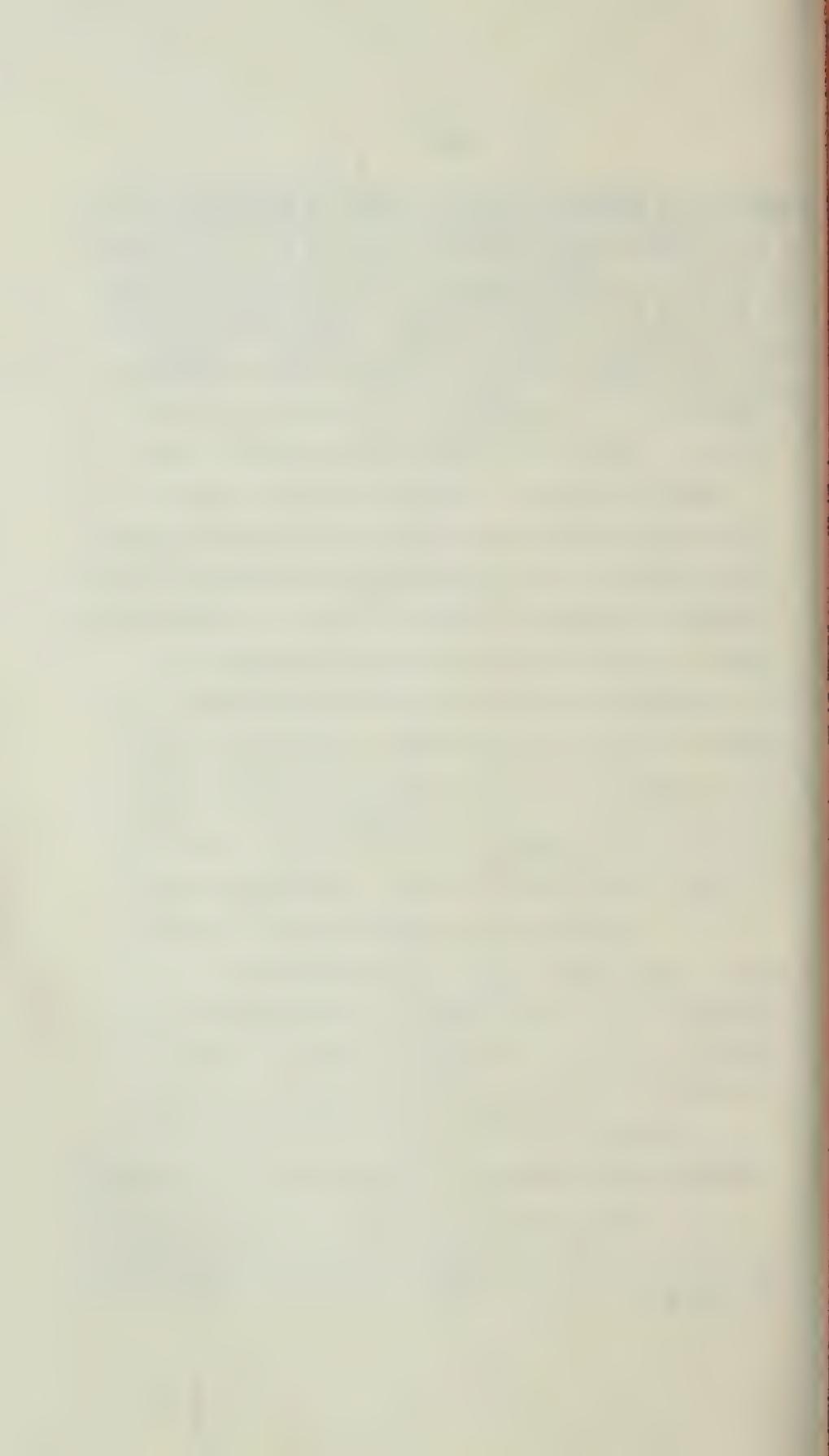
(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation. Mar. 9, 1945, c. 20, Secs. 3, 59 Stat. 34; July 25, 1947, c. 326, 61 Stat. 448.

Section 1014. Applicability of National Labor Relations Act and the Fair Labor Standards Act of 1938

Nothing contained in this chapter shall be construed to affect in any manner the application to the business of

insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938, or the Act of June 5, 1920, known as the Merchant Marine Act, 1920. Mar. 9, 1945, c. 20, Secs. 4, 59 Stat. 34.



No. 22598

MAR 12 1968

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Appellant,

vs.

HAMILTON LIFE INSURANCE  
COMPANY OF NEW YORK and  
FINANCIAL SECURITY LIFE  
INSURANCE COMPANY,

Appellees.

BRIEF OF APPELLEE  
HAMILTON LIFE INSURANCE  
COMPANY OF NEW YORK

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HAMILTON LIFE INSUR-  
ANCE COMPANY OF  
NEW YORK

FILED

AUG 12 1968

WM. B. LUCK, CLERK



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BRIEF OF APPELLEE  
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BRIEF OF APPELLEE  
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COMPANY OF NEW YORK

STATEMENT OF ISSUES

Hamilton Life Insurance Company of New York (hereafter "Hamilton Life") objects to the inclusion of Issue II at page 5 of the brief of Republic National Life Insurance Company (hereafter "Republic National"): "Whether the District Court erred in failing to pass upon the facts of whether there was a written arbitration agreement between the parties and arbitrable issues." In its order of February 15, 1968, the Arizona District Court stated: ". . . this Court being satisfied that on the face of the pleadings there is a written contract involving commerce with

disputed issues under the contract that come within the scope of the arbitration clause contained in the contract . . . ." (R. 101).

Hamilton Life believes that the issues properly before the Court on this appeal are the following:

1. Whether the Arizona District Court properly referred to the New York District Court the question of whether the McCarran Act renders unenforceable the parties' written agreement to arbitrate.
2. Whether the Arizona District Court acted properly under its inherent power to grant a stay of proceedings in that Court pending conclusion of the New York arbitration proceedings.
3. In the alternative only, whether the McCarran Act precludes application of the Federal Arbitration Act to insurance companies.

#### STATEMENT OF THE CASE

This is an appeal from an order of the United States District Court for the District of Arizona granting a motion of defendant Hamilton Life to stay further proceedings in the Arizona Court pending a decision on Hamilton Life's petition for arbitration in the United States District Court for the Southern District of New York, and from an order of the Arizona court denying plaintiff's motion for rehearing. The District Court had jurisdiction under 28 U.S.C. Sec. 1332. The United States Court of Appeals for the Ninth Circuit has jurisdiction of this appeal under 28 U.S.C. Sec. 1292. *Hudson Lumber Co. v. United States Plywood Corp.*, 181 F.2d 929 (9th Cir. 1950).

On September 21, 1965, plaintiff Republic National and defendant Hamilton Life entered into a reinsurance agreement (Exhibit "A" to the complaint), Article XII of which provided for arbitration in New York of all differences and disputes arising under the agreement.\* Differences and disputes did arise. On

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\* The allegations of a parol agreement do not find support in the record, and Hamilton Life objects to the references to such an agreement at pp. 2-3 of Republic National's brief.

July 13, 1967, Republic National filed what purported to be an interpleader action in the United States District Court in Texas against this defendant and others. On October 23, 1967, the Texas court dismissed that action for lack of jurisdiction. Republic National appealed, but abandoned its appeal (Einhorn Affidavit, R. 30). Meanwhile, on July 27, 1967, Hamilton Life made a formal demand for arbitration as provided in the agreement. Without responding to that demand, Republic National instituted this action in Arizona, filing with its complaint a notice of refusal to arbitrate.\* However, Hamilton Life served a notice of appointment of arbitrator upon plaintiff on November 14, 1967 (R. 30), and on December 11, 1967, filed a petition to compel arbitration in United States District Court for the Southern District of New York (R. 32). That proceeding was brought under 9 U.S.C. Sec. 4. On July 30, 1968, Hamilton Life's motion to compel arbitration was granted by the New York court, which found that Republic National "has subjected Hamilton to a barrage of court proceedings in an effort to obtain judicial relief," instead of proceeding to arbitration. The opinion granting arbitration is set out in Addendum C to this brief.

Incidental to the New York action, Hamilton Life filed a motion in the United States District Court for the District of Arizona for a stay of proceedings in that court pending the arbitration sought in New York (R. 10). That motion was granted (R. 83), and plaintiff's motion for rehearing was denied (R. 101). Plaintiff thereupon filed this appeal (R. 103). This Court granted an ex parte stay of the orders of the Arizona court for a few days, then vacated its stay. Republic National thereupon filed with the Clerk of the Supreme Court of the United States a motion to stay the orders of the Arizona Court pending this appeal, and Mr.

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\* Hamilton Life's demand for arbitration and Republic National's notice of refusal to arbitrate, though on file with the District Court, have apparently not been transmitted to this Court. They are set out in Addendum B to this brief.

Justice Black summarily denied Republic National's motion.\* Republic National then filed its opening brief with this Court.

## ARGUMENT

### I. *Introduction.*

Hamilton Life and Republic National entered into a written agreement to arbitrate, and Hamilton Life has brought proceedings for that purpose in the forum of arbitration, New York. The matter proceeded in two jurisdictions, since Republic National had brought suit against Hamilton Life in Arizona. In both courts, Republic National has argued that the McCarran Act renders unenforceable the arbitration agreement of the parties. The essential question before this Court is which District Court should rule upon Republic National's alleged defense to the arbitration proceedings. Hamilton Life contends that the appropriate forum for this defense is the United States District Court of the Southern District of New York, where Hamilton Life has brought an action to enforce arbitration. Hamilton Life further argues that even were the matter to be decided by the Arizona court, Republic National's McCarran Act argument is without substance.

### II. *The Arizona District Court Properly Referred to the New York District Court the Question of Whether the McCarran Act Precludes Enforcement of the Parties' Written Agreement to Arbitrate.*

Republic National argues that under the McCarran Act, Texas law prohibits the enforceability of the parties' agreement to arbitrate. The question before this Court is whether that determination may be made by the court in which arbitration has been sought by Hamilton Life (the United States District Court for the Southern District of New York), or must be made by the court in which Republic National seeks a declaration that it is not liable to Hamilton Life, or for a determination of the

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\* Letter from Clerk of United States Supreme Court to John P. Frank, March 12, 1968.

extent of such liability (the United States District Court for the District of Arizona).\*

The agreement of the parties provides for arbitration of disputes in the State of New York. The Federal Arbitration Act, relevant provisions of which are set out in Addendum A to this brief, makes arbitration agreements of this sort "valid, irrevocable and enforceable." 9 U.S.C. Sec. 2. The court in which a suit is pending which involves issues referable to arbitration "shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement . . ." 9 U.S.C. Sec. 3. If there is a failure to arbitrate, the party aggrieved may apply for a court order to compel arbitration. 9 U.S.C. Sec. 4. That is precisely what has been done by Hamilton Life in this case. The arbitration jurisdictionally must then go forward in the district in which the application is made, by virtue of the express language of the statute and the cases. *Continental Grain Co. v. Dant & Russell, Inc.*, 118 F.2d 967 (9th Cir. 1941). Where, as here, the arbitration agreement requires arbitration in the State of New York, no other jurisdiction can direct the arbitration there except a New York Court. *China Union Lines, Ltd. v. Steamship Co.*, 136 F. Supp. 597 (S.D.N.Y. 1955). Common sense indicates that all alleged defenses against Hamilton Life's right to secure arbitration of the disputes should be brought in the court which has jurisdiction over the arbitration proceedings, the Southern District of New York, and not elsewhere. The precise legal question is whether the federal arbitration statutes and the cases accord with this approach.

The answer is yes. The motion in the Arizona court for a stay of proceedings under Sec. 3 of the Federal Arbitration Act was not a proper occasion for ruling upon disputed matters. In *Tepper Realty Co. v. Mosaic Tile Co.*, 259 F. Supp. 688 (S.D.N.Y.

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\* The New York Court has already made this determination, holding that the arbitration agreement is enforceable. See Addendum C.

1966), the court held that the question of who were the parties to the arbitration agreement was a matter properly to be heard under a motion to compel arbitration under 9 U.S.C. Sec. 4, rather than a motion to stay proceedings under 9 U.S.C. Sec. 3. The court stated:

"Section 3 makes no provision for preliminary trials of issues which have been, or may be, raised in an answer but commands a stay if the claim asserted in the complaint is one which is subject to the arbitration agreement. There can be no question that on its face the claim alleged here is subject to, and within the ambit of, the arbitration agreement. That is enough to satisfy the requirements for a stay under §3." 259 F. Supp. at 693.

This conclusion is reinforced by the rule that the allegations of the party moving for a stay of proceedings must be accepted as true. *In re Pahlberg*, 43 F. Supp. 761, 764 (S.D.N.Y.), *appeal dismissed*, 131 F.2d 968 (2d Cir. 1942). This rule indicates the courts' unwillingness to enter into determinations of questions of fact and law on a motion for a stay of proceedings under 9 U.S.C. Sec. 3.\*

The issues raised by Republic National in the Arizona court constitute a challenge to the jurisdiction of the New York court under the Federal Arbitration Act. But clearly the New York court, the only court which can render a decision on the merits of the arbitration proceedings, is entitled to make its own determination of its jurisdiction. As was held in *McBeath v. Inter-American Citizens for Decency Comm.*, 374 F.2d 359 (5th Cir. 1967), *cert. denied*, 389 U.S. 896, 88 S. Ct. 216, 19 L. Ed. 2d 213 (1967):

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\* See also *Lesser Towers, Inc. v. Roscoe-Ajax Constr. Co.*, 258 F. Supp. 1005 (S.D. Cal. 1966). This case is in part immaterial because it involves questions of removal from a state to a federal court, and a matter of timeliness; but it is also suggestive for various of the dicta which it contains. We read the case to hold that where there is a question of what law is to be applied in interpreting a contract, the court which has assumed jurisdiction of the arbitration proceeding should dispose of all the legal questions. 258 F. Supp. at 1012.

"Undoubtedly, under Rule 12(d) of the Federal Rules of Civil Procedure a court may determine the prerequisites to jurisdiction in advance of the trial on the merits. However, where the factual and jurisdictional issues are completely intermeshed the jurisdictional issues should be referred to the merits, for it is impossible to decide the one without the other." 374 F.2d at 362-63.

The Arizona District Court did decide in the present case that, on the face of the pleadings, the claim was subject to the parties' arbitration agreement. Having made that determination, the court properly held that Republic National's alleged defenses against arbitration should be decided by the only court having jurisdiction of the arbitration—the United States District Court for the Southern District of New York.

### *III. The Arizona District Court Acted Properly Under its Inherent Power to Grant a Stay.*

Wholly apart from the provisions of the Federal Arbitration Act relating to the granting of a stay of proceedings pending arbitration, the Arizona District Court had inherent power to grant such a stay. This inherent power was relied upon in granting a stay of court proceedings pending arbitration in *Nederlandse Erts-Tankersmaatschappij v. Isbrandtsen Co.*, 339 F.2d 440 (2d Cir. 1964). A similar result was reached with respect to an issue allegedly outside the scope of the arbitration agreement in *Tepper Realty Co. v. Mosaic Tile Co.*, *supra*.

Under these decisions, the court, in considering whether the motion for a stay should be granted, need consider only whether the stay will effectively bring about a resolution of the dispute between the parties, and ease the crowding of court dockets. That is surely the case here. Arbitration, if allowed to proceed in New York, will dispose of many issues in the Arizona case, and will

carry out the agreement of the parties as to the manner of the settlement of their disputes.\*

Republic National argues, at pp. 23-24 of its brief, that the decision of the District Court was based upon the Federal Arbitration Act, rather than the court's inherent power to grant a stay. However, the decision of the District Court must be upheld if there is *any* proper basis for the decision, even if the specific rationale used by the court was inappropriate. *J. E. Riley Inv. Co. v. Commissioner*, 311 U.S. 55, 61 S. Ct. 95, 85 L. Ed. 36 (1940); *SEC v. Chenery Corp.*, 318 U.S. 80, 63 S. Ct. 454, 87 L. Ed. 626 (1943).

Because the Arizona District Court had discretion to grant a stay even if it accepted all of Republic National's arguments, its decision should not be disturbed on appeal.

Republic National apparently concedes the inherent power of a court to grant a stay of its own proceedings pending arbitration in another jurisdiction. But Republic National argues, beginning at p. 24 of its brief, that the exercise of such power would have been inappropriate in the present case. Republic National bases its argument on the decision in *Kerotest Mfg. Co. v. C-O-Two Fire Equip. Co.*, 342 U.S. 180, 72 S. Ct. 219, 96 L. Ed. 200 (1952). But that decision, and the line of cases following it, are simply inappropriate to the present lawsuit. In that case, one party sought a declaratory judgment in Delaware, against a party that had instituted a lawsuit in Illinois for an injunction. The Court of Appeals held that the Delaware litigation should be stayed pending determination of the earlier lawsuit filed in Illinois. The court found that nothing would be decided in Delaware that could not also be decided in Illinois, while substantial issues

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\* A stay granted under the inherent powers of the court, without reference to the Federal Arbitration Act, makes the entire McCarran Act argument of Republic National wholly irrelevant to the Arizona proceedings, for that court then does not apply any federal statutes. Republic National could, of course, still raise the McCarran Act issue as a defense against arbitration in the New York court, as it has done.

would remain to be decided in the Illinois court regardless of the outcome of the Delaware action. The Court of Appeals therefore held that the Delaware action should be stayed, an exercise of discretion which the United States Supreme Court declined to upset. The *Kerotest* situation is wholly distinguishable from the present case, in which the Arizona court has no power to enforce the arbitration agreement of the parties, and where the successful completion of arbitration in New York may well dispose of virtually all issues before the Arizona court. The very considerations operative in the *Kerotest* decision thus indicate that the stay of Arizona proceedings pending the completion of arbitration in New York was proper.

This is particularly true where a narrow question such as the effect of the McCarran Act on arbitration proceedings is before the tribunal which can best deal with it—here the court which can enforce arbitration. See, for example, *Humboldt Placer Mining Co. v. Best*, 185 F. Supp. 290 (N.D. Cal. 1960), in which the United States filed condemnation suits in the California District Court. The defendants then instituted contest proceedings before the Bureau of Land Management. The plaintiff brought a complaint for an injunction against those proceedings. A temporary restraining order was granted, and defendants asked the court to vacate that order. The court held:

[W]here a court has jurisdiction of an entire controversy, it may wait until a court or tribunal of more limited jurisdiction adjudicates the issues peculiarly within its competency, and then give binding effect to the decision of such court or tribunal . . ." 185 F. Supp. at 291-92.

This judgment was vacated, 293 F.2d 553 (9th Cir. 1961), but that decision was reversed, 371 U.S. 334, 83 S. Ct. 379, 9 L. Ed. 2d 350 (1963). See also *Lowry & Co. v. S.S. Nadir*, 223 F. Supp. 871 (S.D.N.Y. 1963), staying a court action until arbitration is completed abroad.

The Arizona court clearly had discretion to grant the stay, and its exercise of discretion should not be overturned by this Court.

IV. *The McCarran Act does not Preclude Application of the Federal Arbitration Act to Reinsurance Agreements Between Insurance Companies.*

Plaintiff argues that the McCarran-Ferguson Act (15 U.S.C. Sec. 1011 et seq.) precludes the application of the Federal Arbitration Act to disputes between insurance companies, for such application would invalidate, impair or supersede applicable Texas law. Relevant provisions of that Act are set out in Addendum A. Sec. 1012(b) provides:

"No act of Congress shall be construed to invalidate, impair or supersede any law enacted by any state for the purpose of regulating the business of insurance . . . unless such act specifically relates to the business of insurance . . . ."

The Arizona court did not consider the merits of Republic National's argument, holding that the McCarran Act issue was properly to be considered by the New York District Court, rather than the Arizona District Court. As argued above, the stay of the Arizona proceedings pending arbitration was justifiable under the court's inherent power to grant a stay, and the decision of the lower court should be upheld for that reason, completely irrespective of any considerations of the McCarran Act and the Federal Arbitration Act. But if the Court does feel that this is a proper occasion for considering the McCarran Act issues raised by Republic National, Hamilton Life urges that the McCarran Act does not preclude enforcement of an arbitration agreement entered into by insurance companies.

A. *The Relevant State Law, that of New York, Would Not be Invalidated, Impaired or Superseded by Application of the Federal Arbitration Act.*

As the United States District Court for the Southern District of New York has held in this case, New York law would be applicable to this transaction, because almost all of the significant contracts of the transactions were with New York. The ultimate insureds reside in that state, and it was agreed that arbitration

would take place there. (See Addendum C). Arbitration relates to the law of remedies. *Red Cross Line v. Atlantic Fruit Co.*, 264 U.S. 109, 44 S. Ct. 274, 68 L. Ed. 582 (1924); *Marine Transit Corp. v. Dreyfus*, 284 U.S. 263, 52 S. Ct. 166, 76 L. Ed. 282 (1932). Where the parties agree to arbitration in a particular state, their agreement is governed by the arbitration law of that state. As the Court of Civil Appeals of Texas stated in *Brownwood Mfg. Co. v. Tanenbaum Textile Co.*, 404 S.W.2d 106 (1966):

"When appellants entered into these written contracts providing for arbitration in New York, they were charged with notice of the New York laws pertaining to arbitration and consented to be bound thereby." 404 S.W.2d at 109.

See also *Carrington, The 1965 General Arbitration Statute of Texas*, 20: 21 Sw. L. J. 21, 52 (1966):

"[T]he mere incorporation of an expression indicating that the parties expect or provide that the arbitration shall be held in New York, may be the equivalent of an express agreement that the provisions of the statutes of that state shall apply."

Application of New York law is also supported by the rule that parties to an agreement must be deemed to have intended a valid act. Thus, even if Texas laws do prohibit arbitration, as Republic National argues, the court would not apply Texas law, which would render the parties' agreement invalid, but would rather apply New York law, which would give effect to the agreement to arbitrate. See *Grace v. Orkin Exterminating Co.*, 255 S.W.2d 279 (Tex. Civ. App. 1953):

"It is ordinarily to be implied that parties who have purportedly entered into a contract intended the agreement to be legally effective, and this implication has been frequently resorted to in settling questions of conflicts of laws . . . . We conclude that the parties to the written contract intended their written agreement to be given such legal effect and validity as could be given it, and as an incident of this intention should be taken to have necessarily intended that validity be determined by the system of law which would give effect to the agreement rather

than by a system which would hold it invalid." 255 S.W. at 292-93.

By agreeing to arbitration in New York, the parties have agreed to the applicability of New York laws, rather than Texas laws relating to arbitration. The argument of Republic National, that application of the Federal Arbitration Act would invalidate, impair or supersede Texas laws relating to arbitration is therefore inappropriate; the relevant question is whether the application of the Federal Arbitration Act would impair, invalidate or supersede relevant provisions of New York law.

Application of the Federal Arbitration Act would not have an effect upon New York law prohibited by the McCarran Act. The United States District Court for the Southern District of New York has so held, in the opinion set forth in Addendum C, pp. 37-39. We incorporate that decision herein, and ask that the Court weigh and consider the cases and arguments relied upon by the New York court. That court rejected the argument raised by Republic National, at page 18 of its brief, that under New York law the validity of a contract containing an arbitration clause is to be determined by the courts, not by the arbitrators, unlike proceedings under the Federal Arbitration Act. The New York court held, after examination of the statutes and cases, that New York law was unsettled on the question of who decides whether a contract containing an arbitration clause was induced by fraud, but that regardless of how that question was decided, there would be no conflict with the Federal Arbitration Act so as to bring the McCarran Act into play.

*B. Even if Texas Law Were Relevant, Application of the Federal Arbitration Act Would Not Contradict The McCarran Act.*

This issue, too, has been decided by the United States District Court for the Southern District of New York. Because that court carefully weighed the applicable authorities and arguments, we do not set forth here a repetition of the materials, but instead incorporate the New York decision by reference, and ask that

the Court consider its holding on this issue set forth in Addendum C, pp. 33-35.

### CONCLUSION

The parties to this appeal have agreed in writing to arbitrate their disputes and differences. Proceedings to enforce that arbitration agreement are now under way in New York. The arbitration statutes, the cases, and the interests of judicial administration compel Republic National to raise its defenses against arbitration in the jurisdiction where arbitration is sought, rather than in the District of Arizona. The Arizona District Court recognized this, and stayed its own proceedings pending arbitration in New York. If this was not commanded by the cases and statutes, certainly the Arizona Court had discretion to enter such an order, and it should not be disturbed on appeal. Even if it were necessary to confront Republic National's objections to arbitration on the merits, those objections are unsound. There is simply no reasonable basis upon which it can be asserted that the McCarran Act precludes enforcement of the parties' arbitration agreement under the Federal Arbitration Act.

The orders appealed from should be affirmed.

LEWIS ROCA BEAUCHAMP &  
LINTON

By JOHN P. FRANK  
Attorneys for Appellee  
Hamilton Life Insurance  
Company of New York

August, 1968.

CERTIFICATION

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with the rules.

John P. Frank

ADDENDUM A  
UNITED STATES CODE  
ANNOTATED  
TITLE 9  
ARBITRATION

Section 2. Validity, irrevocability, and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 4. Failure to arbitrate under agreement; petition to United States Court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may

petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof. As amended Sept. 3, 1954, c. 1263, Section 19, 68 Stat. 1233.

**TITLE 15  
COMMERCE AND TRADE  
SECTIONS 1011-1014  
THE McCARRAN-FERGUSON ACT**

**Section 1011. Declaration of policy**

Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States. Mar. 9, 1945, c. 20, Sec. 1, 59 Stat. 33.

**Section 1012. Regulation by State law, Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948**

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: Provided, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law. Mar. 9, 1945, c. 20, Secs. 2, 59 Stat. 34; July 25, 1947, c. 326, 61 Stat. 448.

**ADDENDUM B**

**DEMAND FOR ARBITRATION**

Date: July 27, 1967

TO: Republic National Life Insurance Company  
3988 North Central Expressway  
Dallas, Texas 75204

PLEASE TAKE NOTICE, under Section 7503, Subdivision (c), of the Civil Practice Law and Rules of the State of New York, that pursuant to the provisions of a contract duly entered into between Republic National Life Insurance Company and Hamilton Life Insurance Company of New York on September 21, 1965, which contract provides as follows:

**"ARTICLE XII      ARBITRATION**

1. All disputes and differences between the two contracting parties upon which an amicable understanding cannot be reached are to be decided by arbitration and the arbitrators shall place a liberal construction upon this agreement free from legal technicalities, for the purpose of carrying out its evident intent.

2. The court of arbitrators, which is to be held in the city where the home office of CEDING COMPANY is domiciled, shall consist of three arbitrators who must be officers of Life insurance companies familiar with the reinsurance business, other than the two parties to this agreement. One of the arbitrators is to be appointed by CEDING COMPANY, the second by REPUBLIC NATIONAL and the third is to be selected by these two representatives before the beginning of the arbitration. Should the two arbitrators be unable to agree upon the choice of a third, the appointment shall be left to the president of the American Life Convention.

3. The arbitrators are not bound by any rules of law. They shall decide by a majority of votes and from their written decision there can be no appeal. The cost of arbitration, including the fees of the arbitrators, shall be borne by the losing party unless the arbitrators shall decide otherwise."

Hamilton Life Insurance Company of New York hereby demands arbitration thereunder.

**NATURE OF DISPUTE:** On September 21, 1965, a group reinsurance agreement was entered into by Hamilton and Republic National, under which it was agreed that Hamilton would cede to Republic National and Republic National would accept liability for certain group life insurance claims paid by Hamilton, to the extent of 80% thereof. Pursuant to the said reinsurance agreement, Hamilton ceded to Republic National and Republic National accepted certain business under group policies of life insurance. Thereafter, Hamilton paid various claims under the group insurance contracts ceded to and accepted by Republic National and Republic National's share thereof under the above-mentioned reinsurance agreement is \$278,023.41. Upon such payment by Hamilton, Republic National became obligated to pay to Hamilton the sum of \$278,023.41. Republic National has denied that it is obligated to Hamilton in the said amount or in any amount and has refused to make payment to Hamilton.

**CLAIM OR RELIEF SOUGHT:** Hamilton seeks an award directing payment to it by Republic National of the sum of \$278,023.41.

**PLEASE TAKE FURTHER NOTICE,** that unless within ten days after service of this Notice of Intention to Arbitrate, you apply to stay the arbitration herein, you shall thereafter be precluded from objecting that a valid agreement was not made or has not been complied with and from asserting in court the bar of a limitation of time.

HEARING LOCALE DEMANDED: New York City.

Yours, etc.,

ARANOW, BRODSKY, BOHLINGER,  
EINHORN & DANN

By: /s/ Herbert A. Einhorn  
A Member of the Firm

Attorneys for Hamilton Life Insurance  
Company of New York  
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212 687-6343

IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF ARIZONA

REPUBLIC NATIONAL LIFE  
INSURANCE COMPANY,

Plaintiff,

vs.

FINANCIAL SECURITY LIFE  
INSURANCE COMPANY and  
HAMILTON LIFE INSURANCE  
COMPANY OF NEW YORK,

Defendants.

No. CIV-6501  
PHX.

NOTICE OF  
REFUSAL TO  
ARBITRATE

Republic National Life Insurance Company, Plaintiff in the captioned action, having previously received written demand for arbitration as specified below, relative to such demand states:

I

Petitioner has been served with a "Demand for Arbitration" by attorneys for Hamilton Life Insurance Company, one of the Defendants in this cause. A true and correct copy thereof is attached hereto marked Exhibit "1".

II

That suit in the nature of interpleader was filed in the United States District Court for the Northern District of Texas on July 13, 1967. That on October 23, 1967 said court entered its order dismissing the cause of action to which order Plaintiff gave its notice of appeal within the time period prescribed. Subsequently suit was filed by Plaintiff in the United States District Court for the District of Arizona on November 3, 1967. A true and correct copy of the complaint marked Exhibit "2" is attached hereto and made a part hereof, the same as though set out herein in full. By reason of such suit, exclusive jurisdiction to try all

matters at issue resides in the Court in which the complaint is filed and no demand for arbitration may properly oust the jurisdiction of the court already attached.

### III

The reinsurance contract between Republic National Life Insurance Company and Hamilton Life Insurance Company is a Texas contract and must be construed in accordance with the laws of Texas which prohibit arbitration contracts and particularly those pertaining to insurance.

### IV

The purported agreement to arbitrate is invalid and illegal on its face for reasons that are self-apparent.

### V

Further, Republic National Life Insurance Company has alleged in its complaint in this action that the contract referred to in the demand for arbitration is itself now invalid and unenforceable and revoked or subject to revocation under the circumstances stated in the complaint, all of which under the law precludes arbitration of the issues and controversies referred to in the demand for arbitration.

### VI

The controversies stated in the complaint arise between Republic National Life Insurance Company, Hamilton Life Insurance Company of New York, and Financial Security Life Insurance Company; and no agreement exists making disputes arising between these three parties subject to arbitration.

WHEREFORE, Republic National Life Insurance Company respectfully refuses to honor the demand for arbitration previously served upon it as stated above, and requests that the court make its order directing the time and method of service of this notice upon the Defendants in this cause who have not appeared to date and are not yet in default, together with such

other and further orders relative to the matters stated as are appropriate in the law or equity.

Respectfully submitted,

CARSON MESSINGER ELLIOTT  
& RAGAN

By ROBERT W. HOLLAND

1400 Guaranty Bank Building  
3550 North Central Avenue  
Phoenix, Arizona 85012

## ADDENDUM C

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

HAMILTON LIFE INSURANCE  
COMPANY OF NEW YORK,

Petitioner,

- against -

REPUBLIC NATIONAL LIFE  
INSURANCE COMPANY,

Respondent.

67 Civ. 4855

## OPINION

## APPEARANCES:

ARANOW, BRODSKY, BOHLINGER,  
EINHORN & DANN  
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HERBERT A. EINHORN  
ANTHONY L. TERSIGNI  
of Counsel.

SIMPSON THACHER & BARTLETT  
Attorneys for Respondent

THOMAS G. NASH, JR.  
CARSON MESSINGER ELLIOT  
LAUGHLIN & RAGAN  
ROBERT W. HOLLAND  
of Counsel.

## HERLANDS, District Judge:

Novel and important questions of federal-state relations in accommodating the Federal Arbitration Act, 9 U.S.C. § 1 et seq. with the McCarran-Ferguson Insurance Regulation Act,

15 U.S.C. § 1011 et seq. are raised by the petitioner's motion and the respondent's cross-motion.

Petitioner Hamilton Life Insurance Company of New York (Hamilton), moves for an order, pursuant to 9 U.S.C. § 44<sup>1</sup> (the Federal Arbitration Act) directing the respondent, Republic National Life Insurance Company (Republic), to proceed to arbitration. Republic has cross-moved, pursuant to Fed. R. Civ. P. 12(b), to dismiss the petition on the following three grounds:

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<sup>1</sup>9 U.S.C. § 4 provides:

"§ 4. Failure to arbitrate under agreement; petition to United States Court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination.

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be in default, may, except in cases of admiralty, on or before the return of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof."

(1) that the Court lacks subject matter jurisdiction; (2) that the Court lacks *in personam* jurisdiction over Republic; and (3) that Hamilton has failed to join an indispensable party. As alternative relief, Republic seeks a stay of all proceedings pending the determination by the Court of Appeals for the Ninth Circuit of an appeal in a related proceeding.

On September 21, 1965, Republic and Hamilton entered into a group reinsurance agreement. This provided that Republic would reinsure a certain percentage of the risks on group life insurance policies written by Hamilton covering civil service employees in the New York City area. The group reinsurance agreement is contained in a standard form of reinsurance contract furnished by Republic. It was executed in New York City by an officer of Hamilton, who then mailed it to Republic's office in Dallas, Texas for signature. (Affidavit of Robert H. Autenreich, sworn to December 12, 1967, pp. 2-3). After the agreement was executed, additional negotiations occurred. As a result, there was a change in the first year administrative charge on ceded business. This change was made in the original reinsurance agreement, which was first initialed by an officer of Republic in Dallas, Texas and then by an officer of Hamilton in New York City, in October, 1965. (Autenreich Affidavit, p. 3 and Exhibit 1 attached thereto).

The reinsurance agreement contains the following broad arbitration clause:

#### "ARTICLE XII ARBITRATION

1. All disputes and differences between the two contracting parties upon which an amicable understanding cannot be reached are to be decided by arbitration and the arbitrators shall place a liberal construction upon this agreement free from legal technicalities, for the purpose of carrying out its evident intent.

2. The court of arbitrators, which is to be held in the city where the home office of CEDING COMPANY [Hamilton] is domiciled, shall consist of three arbitrators who must be officers

of Life insurance companies familiar with the reinsurance business, other than the two parties to this agreement. One of the arbitrators is to be appointed by CEDING COMPANY [Hamilton], the second by REPUBLIC NATIONAL and the third is to be selected by these two representatives before the beginning of the arbitration. Should the two arbitrators be unable to agree upon the choice of a third, the appointment shall be left to the president of the American Life Convention.

3. The arbitrators are not bound by any rules of law. They shall decide by a majority of votes and from their written decision there can be no appeal. The cost of arbitration, including the fees of the arbitrators, shall be borne by the losing party unless the arbitrators shall decide otherwise."

Disputes having arisen between the parties, on July 27, 1967 Hamilton served a Demand For Arbitration in New York City on Republic. The Demand For Arbitration recited that Hamilton had paid various claims under group insurance contracts ceded to and accepted by Republic and that by virtue of the reinsurance agreement Republic was obligated to pay Hamilton the sum of \$278,023.41. (Exhibit 1 to Affidavit of Herbert A. Einhorn, sworn to December 11, 1967).

On November 14, 1967, Hamilton served a Notice of Appointment of Arbitrator, which also demand that Republic select an arbitrator pursuant to the terms of the reinsurance agreement. (Exhibit 2 to Einhorn Affidavit). Republic, however, has refused to proceed to arbitration. Instead, it has subjected Hamilton to a barrage of court proceedings in an effort to obtain judicial relief.

On July 14, 1967, Republic commenced an action against Hamilton based on the agreement in issue in the United States District Court for the Northern District of Texas. The action was dismissed for lack of jurisdiction on October 23, 1967. Republic appealed from this dismissal on October 30, 1967. On November 17, 1967, Republic voluntarily discontinued its appeal.

On November 3, 1967, Republic commenced a second action against Hamilton, this time in the United States District Court for the District of Arizona. Service of the summons and complaint

in that action was effected on Hamilton on November 20, 1967.

On December 11, 1967, Hamilton filed in this Court a petition to compel arbitration (Hamilton's motion now before the Court), which was brought on for hearing on December 26, 1967 by a notice of motion dated December 12, 1967.

Republic did not file an answer to the petition herein or request an adjournment of the proceedings in this Court. Instead, on December 20, 1967, Republic obtained, *ex parte*, from the United States District Court for the District of Arizona a temporary restraining order prohibiting Hamilton from proceeding before this Court. This order was extended on December 29, 1967. On January 9, 1968, a preliminary injunction against proceeding in this Court was issued in order to afford the United States District Court for the District of Arizona an opportunity to consider the matter fully.

On January 29, 1968 the United States District Court for the District of Arizona quashed its injunction and granted Hamilton a stay of all further proceedings in Arizona pending this Court's determination of the present application for an order directing arbitration.

On February 2, 1968, Republic moved in the Arizona federal district court for a rehearing or for a stay of its order quashing the preliminary injunction against proceeding in this Court pending appeal. On February 15, 1968, the Arizona court adhered to its prior determination but directed that no proceedings take place in the Southern District of New York until February 27, 1968 in order to allow Republic to apply to the Ninth Circuit Court of Appeals for a stay.

On February 19, 1968, Republic applied *ex parte* to said Court of Appeals for a stay. On February 21, 1968, the Ninth Circuit stayed until March 4, 1968 the dissolution of the preliminary injunction against proceeding in the Southern District of New York to allow Hamilton to be heard on Republic's application for a

stay pending appeal. Subsequently, on March 4, 1968, the Ninth Circuit vacated its temporary stay.

On March 7, 1968, Republic applied to the United States Supreme Court for a temporary stay. On March 8, 1968, this application was denied by Mr. Justice Black.

## I

Whether the McCarran-Ferguson Insurance Regulation Act, 15 U.S.C. §1011 et seq. (hereinafter the McCarran-Ferguson Act) prevents the petitioner from compelling arbitration of this dispute pursuant to §4 of the Federal Arbitration Act<sup>2</sup> is the threshold and crucial question. For the reasons that follows, this Court answers that question in the negative.

In *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), the Supreme Court decided that the business of insurance was commerce and therefore subject to federal regulatory legislation, specifically the anti-trust laws. *South-Eastern Underwriters* reversed the pre-existing rule that the business of insurance was not commerce and hence subject only to state regulation. See *Paul v. Virginia*, 75 U.S. 168 (1868); *New York Life Insurance Co. v. Deer Lodge County*, 231 U.S. 495 (1913).

The McCarran-Ferguson Act was enacted in 1945 in order to "allay doubts" that *South-Eastern Underwriters* impaired "the continuing power of the States to tax and regulate the business of insurance." *FTC v. Travelers Health Ass'n*, 362 U.S. 293, 299 (1960); *State Board of Insurance v. Todd Shipyards Corp.*, 370 U.S. 451, 452 (1962); *Maryland Casualty Co. v. Cushing*, 347

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<sup>2</sup> It is uncontested that the agreement in issue satisfies the jurisdictional requirements of the Act. Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides that a written arbitration provision "in \* \* \* a contract evidencing a transaction involving commerce \* \* \* shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." The agreement in issue involving interstate transactions between companies of different states is manifestly one "evidencing a transaction involving [interstate] commerce."

U.S. 409, 413 (1954); *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408, 429-433 (1946).

The purpose and scope of the statute is summed up in the House Report on the bill:

"It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association* case. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the State, subject always, however, to the limitations set out in the controlling decisions of the Supreme Court . . . which hold, *inter alia*, that a State does not have power to tax contracts of insurance or reinsurance entered into outside its jurisdiction by individuals or corporations resident or domiciled therein covering risks within the State or to regulate such transactions in any way." H.R. Rep. No. 143, 79th Cong., 1st Sess. 3 (1945).

The Congressional policy is enunciated in a prefatory section of the Act stating:

"Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress should not be construed to impose any barrier to the regulation or taxation of such business by the several States." 15 U.S.C. §1011.

Section 2(b), 15 U.S.C. §1012(b)—the statutory section central to the resolution of the problem now before the Court—provides:

"No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, . . . the Sherman Act . . . the Clayton Act and . . . the Federal Trade Commission Act . . . shall be applicable to the business of insurance to the extent that such business is not regulated by State law."

Respondent submits that §2(b) of the McCarran-Ferguson Act exempts the business of insurance from the coverage of all federal statutes which do not specifically state that their provisions are applicable to insurance. Because there is no such specification in the Federal Arbitration Act, respondent argues that that statute is not applicable to this insurance case and, consequently, that there is no subject matter jurisdiction to entertain the petition.

Disputing the basic premises underlying the respondent's position, the petitioner contends that the controlling and precise inquiry is whether the Federal Arbitration Act invalidates, impairs or supersedes any conflicting State law enacted for the purpose of regulating the insurance business. In the petitioner's view the Federal Arbitration Act has no such invalidating, impairing or superseding effect in the instant case; ergo, it is not rendered inapplicable by the McCarran-Ferguson Act. But the petitioner does not stake its case entirely on that proposition.

Assuming *arguendo* that the McCarran-Ferguson Act renders the Federal Arbitration Act inapplicable, the petitioner adopts diversity of citizenship as the predicate for this Court's jurisdiction to compel arbitration pursuant to State law. It is the petitioner's claim that this case is controlled by New York law, under which the parties' agreement to arbitrate is valid and specifically enforceable.

The primary issue to be resolved may be broadly formulated in these terms: to what extent does the McCarran-Ferguson Act limit the operation of federal statutes (such as the Federal Arbitration Act) that do not by their terms specifically apply to the business of insurance? The plain and unambiguous statutory language is persuasive evidence that the McCarran-Ferguson Act was not intended to preclude the application of these federal statutes to insurance *unless* they invalidate, impair or supersede applicable State legislation regulating the business of insurance. However, in reaching this conclusion, the Court does more than simply follow the route of statutory language; it seeks to effectuate the

Act's fundamental objective and dominant intention. Judge Learned Hand's celebrated dictum bears repetition: "it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish whose sympathetic and imaginative discovery is the surest guide to their meaning." *Cabell v. Markham*, 148 F. 2d 737, 739 (2d Cir.), aff'd 326 U.S. 404 (1945).

The primary legislative purpose of the McCarran-Ferguson Act was to reaffirm the States' power to regulate insurance (subject to constitutional limitations) and to ensure that state regulatory schemes would not be impaired and overridden except by specific and explicit Congressional enactments. There is no discernible evidence of a legislative intention that, in the absence of conflicting state regulatory legislation, federal statutes (such as the Federal Arbitration Act) would be inapplicable to the business of insurance. This view is brought into sharp focus by decisions interpreting the McCarran-Ferguson Act that have upheld federal law despite conflicting state statutes. *Maryland Casualty Co. v. Cushing*, *supra*, 347 U.S. at 412-413 (Federal Maritime Law—"The question whether application of the [Louisiana] direct action statute conflicts with federal maritime law is not touched by the *South-Eastern Underwriters* case. In the face of this unequivocal expression of congressional meaning, the statute cannot be read as doing something that Congress has told us it was not intended to do. The McCarran Act is not relevant here."); *Sears Roebuck and Co. v. All States Life Insurance Co.*, 246 F. 2d 161, 172 (5th Cir. 1957) (Lanham Act—"There is nothing in the McCarran Act that limits the right of the owner of a trade or service name to seek redress in the federal courts merely because the approval of the name of the infringing insurance company is part of the duties of the state board."); *Zachman v. Erwin*, 186 F. Supp. 691, 694 (S.D.Tex. 1960) (Securities Act of 1933—"That statute [the McCarran-Ferguson Act] does not preclude application of the Securities Act to the insurance business since there is no indication

that it invalidates, impairs or supersedes any law of the State of Texas regulating the insurance business.”).

*SEC v. National Securities Inc.*, 387 F.2d 25 (9th Cir. 1967), affirming, 252 F. Supp. 623 (D.Ariz. 1966), upon which respondent principally relies, does not dictate a contrary result. In that case, the Securities and Exchange Commission sought to invalidate the merger of two stock life insurance companies on the ground that the anti-fraud provisions of the Securities Exchange Act of 1934 were violated. The District Court merely held that application of the Federal Act “would at least ‘impair’, if not ‘invalidate’ or ‘supersede’” an Arizona statute enacted for the purpose of regulating the business of insurance, which contains the specific requirement that any proposed merger of insurance companies must be approved by the state director of insurance. (252 F. Supp. at 626). The Court of Appeals noted that the State of Arizona had “affirmatively asserted its power to regulate the merger of insurance companies” (387 F.2d at 31) and that the legislative history of the 1964 amendments to the Securities Acts indicate that the States were to “be given an opportunity to demonstrate their ability to effectively protect the investors as well as the policyholders.” (1964 U.S. Code Cong. & Admin. News, p. 3022, quoted in 387 F.2d at 31, n. 3). The Court of Appeals, therefore, affirmed the District Court’s holding that application of the Securities Exchange Act of 1934 would impair, invalidate or supersede the Arizona law. (387 F.2d at 32). The Court did not hold that the Securities Exchange Act of 1934 was inapplicable for the reason that it does not contain a provision making it applicable to insurance. What National Securities, Inc. did hold was that the federal statute did not govern because it impaired a detailed state regulatory scheme specifically and directly aimed at the insurance business.

Next to be considered is the question whether there is any State law enacted for the purpose of regulating insurance which would be invalidated, impaired or superseded if the Federal Ar-

bitration Act is applied to the present case. The only two States having an interest in the present controversy are Texas and New York. Respondent asserts that Article 224 of the present Texas Arbitration Statute is in direct conflict with the Federal Arbitration Act. This Texas provision renders enforceable written agreements to arbitrate future as well as existing disputes but provides that "none of the provisions of this Act shall apply to . . . any contract of insurance or any controversy thereunder." 10 *Vernon's Civil Stats.* Art. 224 (1967 Supp.). However, this provision is applicable only to arbitration agreements made after January 1, 1966 and, therefore, would not apply to the instant agreement, which was executed in September, 1965. Id. Art. 238-3 (1967 Supp.). Furthermore, the agreement in question is a contract of reinsurance between two insurance companies, not a standard insurance contract; and the present statute was enacted to protect Texas insureds from being forced to accept insurance policies—particularly "uninsured motorist" policies—containing arbitration clauses. See, Note 44 *Texas L. Rev.* 372, 373 (1965); P. Carrington, *The 1965 General Arbitration Statute of Texas*, 20 *Southwestern L. J.* 21, 38 (1966).

The Texas General Arbitration Act in force at the time the agreement in issue was executed provides that, while agreements to arbitrate existing controversies would be enforced by the courts of Texas, agreements to arbitrate future disputes would not be judicially enforced. 10 *Vernon's Civil Stats.* Arts. 224-238 (1959 ed.).

Furthermore, this statute is not a "law enacted by any State for the purpose of regulating the business of insurance" within the meaning of § 2(b) of the McCarran-Ferguson Act. The Texas statute is a codification of an old common-law rule, whose purpose was not to regulate the insurance business but rather to preserve the jurisdiction of the courts. See, Dougherty and Graf, *Should Texas Revise Its Arbitration Statutes?*, 41 *Texas L. Rev.* 229 (1962).

Another salient aspect of interpretation is illuminated by those cases which, in construing the proviso to § 2(b) of the McCarran-Ferguson Act, have held that State "regulation" means regulation by the State within whose borders the activity in question has its operative force. In *FTC v. Travelers Health Ass'n*, 362 U.S. 293, 300, 301 (1960), the Supreme Court pointedly stated:

"... [I]t is clear that Congress viewed state regulation of insurance solely in terms of regulation by the law of the State where occurred the activity sought to be regulated. There was no indication of any thought that a State could regulate activities carried on beyond its own borders.

\* \* \*

The three Senate conferees, Senators McCarran, O'Mahoney and Ferguson, repeatedly emphasized that the provision did not authorize state regulation of extraterritorial activities."

Accord: *United States v. Chicago Title and Trust Co.*, 242 F. Supp. 56, 60 (N.D. Ill. 1965) ("The Supreme Court decisions would also indicate the inability of the states to affect matters extraterritorially.").

There is no discernible reason why State "regulation" should be defined differently in § 2(b) of the McCarran-Ferguson Act itself. The legislative history of § 2(b) strongly substantiates the proposition that a State is not empowered to regulate interstate insurance practices which have their situs outside its borders. See H.R. Rep. No. 143, 79th Cong., 1st Sess. 3 (1945). It is this Court's opinion that the agreement herein between the petitioner, a New York corporation and the respondent, a Texas corporation, provides for arbitration in New York City of disputes arising under a contract of reinsurance on group life insurance policies written on New York municipal employees; and that application of the Texas statute to prohibit the submission of this extraterritorial dispute to arbitration in New York City would not be "regulation" within the meaning of § 2(b) of the McCarran-Ferguson Act.

Traditional conflict of laws rules also support the Court's foregoing conclusion. If the Federal Arbitration Act were not applicable to the present case, this Court would have jurisdiction by virtue of diversity of citizenship<sup>3</sup> to decide this case under State law. *Metro Industrial Painting Corp. v. Terminal Construction Co.*, 287 F.2d 382, 388, N.3 (2d Cir.) (Lumbard, C.J., concurring), cert. denied, 368 U.S. 817 (1961); *Sinva, Inc. v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 253 F.Supp. 359, 363 (S.D.N.Y. 1966); *Formigli Corp. v. Alcar Builders Inc.*, 329 F.2d 79, 81 (3d Cir. 1964); *O'Meara v. Texas Gas Transmission Corp.*, 230 F.Supp. 788, 790 (N.D.Ill. 1964); *Cook v. Kuljian Corp.*, 201 F.Supp. 531, 535 (E.D.Pa. 1962). Cf. *Boston & Maine Corp. v. Chicago, B & Q RR Co.*, 381 F.2d 365 (2d Cir. 1967).

Under *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487 (1941), this Court would apply New York choice-of-law rules to determine whether Texas or New York law is applicable to the instant dispute. For conflicts purposes, New York treats arbitration as being part of its "law of remedies" and, therefore, the law of the forum (New York) would govern. *Matter of Gantt*, 297 N.Y. 433, 438-439 (1948); *Metro Industrial Painting Corp.*

<sup>3</sup> Respondent's contention that, absent the Federal Arbitration Act, this Court lacks subject matter jurisdiction is rejected. The Federal Arbitration Act does not create an independent basis for federal jurisdiction. Apart from the requirements of the Act, diversity of citizenship or a federal question is requisite for federal jurisdiction. *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 408 (2d Cir. 1959), cert. dismissed, 364 U.S. 801 (1960); *Krauss Bros. Lumber Co. v. Louis Bossert & Sons*, 62 F.2d 1004, 1006 (2d Cir. 1933) (L.Hand, J.); *Metro Industrial Painting Corp. v. Terminal Construction Co.*, 287 F.2d 382, 384 (2d Cir.), cert. denied, 368 U.S. 817 (1961); *Pock v. New York Typographical Union No. 6*, 223 F.Supp. 181, 183 (S.D.N.Y. 1963); *Victorias Milling Co. v. Hugo Neu Corp.*, 196 F.Supp. 64, 69-70 (S.D.N.Y. 1961); *Local 1416 v. Jostens, Inc.*, 250 F.Supp. 496, 499 (D.Minn. 1966); See Committee on Commerce, Trade & Commercial Law, *The United States Arbitration Act and its Application*, 11 A.B.A.J. 153, 154 (1925).

In the present case, there is diversity of citizenship inasmuch as Hamilton is a citizen of New York and Republic is a citizen of Texas.

v. *Terminal Construction Co.*, *supra*, 287 F.2d at 388, n.3 (concurring opinion); *Sinva, Inc. v. Merrill, Lynch, Pierce, Fenner & Smith*, *supra*, 253 F.Supp. at 364.

Even under the more modern grouping of contracts choice-of-law rule applied by New York to contracts generally, See *Auten v. Auten*, 308 N.Y. 155 (1954), New York law would be applicable as almost all the significant contacts of the transaction were with New York,— where the ultimate insureds reside and where it was agreed arbitration was to take place.

Before § 2(b) of the McCarran-Ferguson Act could become operative, State law *applicable* to the present case must be invalidated, impaired or superseded by the Federal Arbitration Act. Because Texas law would not be applicable even if there were no Federal Arbitration Act, any impairment of the Texas Arbitration Statute would not pose a McCarran-Ferguson Act problem.

Nor is any New York law enacted for the purpose of regulating the business of insurance invalidated, impaired or superseded by the application to this case of the Federal Arbitration Act. The New York Arbitration Act—which is substantially similar to the Federal Arbitration Act—provides that written agreements to arbitrate existing and future controversies are valid and enforceable. N.Y.C.P.L.R. § 7501. Moreover, there is no prohibition against arbitrating disputes arising under contracts of reinsurance.

The only possible difference between the New York and Federal Arbitration Acts relevant to the instant case concerns the question of the arbitrability of a claim that the reinsurance agreement was fraudulently induced. Such an allegation is made by the respondent in paragraph 18 of its answer.

Under federal law, where there is a broad, separable arbitration provision and a party alleges fraud in the inducement of the contract generally—as opposed to fraud in the inducement of the arbitration clause itself—this issue is reserved for the arbitrators and not for the Court. *Prima Paint Corp. v. Flood &*

*Conklin Mfg. Co.*, 388 U.S. 395, 403-404 (1967); *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 410 (2d Cir. 1959), cert. dismissed, 364 U.S. 801 (1960); *El Hoss Engineering & Transport Co. v. American Independent Oil Co.*, 289 F.2d 346, 349 (2d Cir. 1961); *Petition of Kinoshita & Co.*, 287 F.2d 951 (2d Cir. 1961).

In New York, the law "is not entirely clear." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, *supra*, 388 U.S. at 400, n. 3. Most of the reported cases state that a claim of fraud in the inducement of the contract is an issue for the Court and not for the arbitrators. *Matter of Exercycle Corp.*, 9 N.Y. 2d 329, 334, 214 N.Y.S. 2d 353, 356 (1961); *Matter of Wrap-Vertiser*, 3 N.Y. 2d 17, 163 N.Y.S. 2d 639 (1957) (dictum). On the other hand, there is authority holding that, if the arbitration clause is sufficiently broad, the issue of fraudulent inducement of the contract is a question for the arbitrators. *Matter of M. W. Kellogg Co.*, 9 App. Div. 2d 744, 192 N.Y.S. 2d 869 (1st Dep't 1959); *Fabrex Corp. v. Winard Sales Co.*, 200 N.Y.S. 2d 278 (N.Y.Co. 1960); *Matter of Amphenol Corp.*, 49 Misc. 2d 46, 266 N.Y.S. 2d 768 (N.Y.Co. 1965), aff'd mem., 25 App. Div. 2d 497, 267 N.Y.S. 2d 477 (1st Dep't 1966).

If New York law allows the issue of fraud in the inducement of the contract to be arbitrated, there is no conflict with the Federal Arbitration Act. But even if New York law requires this particular issue to be judicially resolved, there is no McCarran-Ferguson Act problem. The New York law on arbitrability is not specifically directed to the insurance business; nor is it intended to proscribe or permit "certain conduct on the part of insurance companies." *California League of Independant Insurance Producers v. Aetna Casualty & Surety Co.*, 175 F.Supp. 857, 860 (S.D.Cal. 1959). It follows that the New York law on arbitrability cannot be considered a state law enacted for the purpose of regulating the business of insurance within § 2(b) of the McCarran-Ferguson Act. In fact (as noted earlier in this

opinion), the purpose and scope of the McCarran-Ferguson Act have been narrowly construed; and federal law has been applied even where there is conflicting state law applicable to the business of insurance. *Maryland Casualty Co. v. Cushing, supra*, 374 {sic} U.S. 409 (Federal Maritime Law not rendered inapplicable by Louisiana direct action statute permitting certain suits against insurance companies); *Sears Roebuck & Co. v. All States Life Insurance Co., supra*, 246 F.2d 161 (Lanham Act not displaced by Texas Insurance Code provision requiring approval of the names of insurance companies by the Texas Board of Insurance Commissioners and a finding that such names were not likely to mislead the public.).

This Court holds that the McCarran-Ferguson Act presents no barrier to applying the Federal Arbitration Act to the present case. The respondent's cross-motion to dismiss the petition herein for lack of subject matter jurisdiction is denied.

## II

This Court next considers the respondent's claim that the petition should be dismissed because the Court lacks in personam jurisdiction. This contention is without merit.

A foreign defendant's agreement to arbitrate in New York constitutes a submission to the jurisdiction of this Court to compel arbitration pursuant to § 4 of the Federal Arbitration Act. This was the holding in *Farr & Co. v. Cia Intercontinental de Navegacion*, 243 F.2d 342, 347 (2d Cir. 1957). Accord: *Victory Transport Inc. v. Comisaria General*, 232 F.Supp. 294, 295 (S.D.N.Y. 1963), *aff'd* 336 F.2d 354, 363 (2d Cir. 1964).

The arbitration agreement herein provides that arbitration shall "be held in the city where the home office of Ceding Company [Hamilton] is domiciled." (Article XII of Reinsurance Agreement). Hamilton, the petitioner, is a New York corporation, whose principal place of business is in New York City. (Petition To Compel Arbitration, ¶1). Under the rule enunciated in *Farr & Co.*, it is clear that, by agreeing to arbitrate in New York,

the respondent must be deemed to have consented to the jurisdiction of this Court to compel such arbitration.

The respondent further argues that the service of process effectuated in this case is a nullity because the respondent was not served within the territorial limits of the State of New York as required by Rule 4(f)<sup>4</sup> of the Federal Rules of Civil Procedure. The respondent was personally served at its home office in Dallas, Texas by the United States Marshal. In addition, the respondent was served by certified mail, return receipt requested, on December 14, 1967. (See Affidavit of Alfred Miller, sworn to March 14, 1968, p.2.).

In *Farr & Co. v. Cia Intercontinental de Navegacion, supra*, 243 F.2d 342, 348, the Court rejected the identical contention and upheld the sufficiency of service by registered mail. The Court stated that § 4 of the Federal Arbitration Act incorporates Rule 4(d)(7)<sup>5</sup> of the Federal Rules of Civil Procedure and

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<sup>4</sup> Rule 4(f) of the Federal Rules of Civil Procedure provides:

"(f) *Territorial Limits of Effective Service.* All process other than a subpoena may be served anywhere within the territorial limits of the state in which the district court is held, and, when authorized by a statute of the United States or by these rules, beyond the territorial limits of that state. In addition, persons who are brought in as parties pursuant to Rule 13(h) or Rule 14, or as additional parties to a pending action pursuant to Rule 19, may be served in the manner stated in paragraphs (1)-(6) of subdivision (d) of this rule at all places outside the state but within the United States that are not more than 100 miles from the place in which the action is commenced, or to which it is assigned or transferred for trial; and persons required to respond to an order of commitment for civil contempt may be served at the same places. A subpoena may be served within the territorial limits provided in Rule 45."

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<sup>5</sup> Rule 4(d)(7) of the Federal Rules of Civil Procedure provides:

"(7) Upon a defendant of any class referred to in paragraph (1) or (3) of this subdivision of this rule, it is also sufficient if the summons and complaint are served in the manner prescribed by any statute of the United States or in the manner prescribed by the law of the state in which the district court is held for the service of summons or other like process upon any such defendant in an action brought in the courts of general jurisdiction of that state."

permits State methods of serving process to be used to compel specific performance of arbitration agreements. Rule 4(f) which relates solely to federal service of process was held not to bar the use of State methods of service, pursuant to Rule 4(d)(7). Applicable New York law holds that "consent to jurisdiction includes consent to service by any method consistent with due process." *Petrol Shipping Corp. v. Kingdom of Greece*, 360 F.2d 103, 107 (2d Cir.), cert. denied, 385 U.S. 931 (1966). Service of process in the present case is unquestionably valid under New York law.

The respondent's cross-motion to dismiss for lack of in personam jurisdiction is denied.

### III

The respondent also seeks to dismiss the petition on the ground that the petitioner has failed to join an indispensable party. The respondent asserts that the reinsurance agreement entered into in September, 1965 was actually tripartite in nature and "was evidenced in part by two separate agreements," one between the petitioner and the respondent and the other between the respondent and Financial Security Life Insurance Company. (Affidavit of Thomas G. Nash, Jr., sworn to March 11, 1968, p.2.). By the terms of this tripartite agreement, the petitioner would cede to the respondent 80% of the risks written, provided that the respondent would cede 80% of that amount to Financial Security Life Insurance Company. (Affidavit of William A. Boles, sworn to January 3, 1968, p.1, attached as Exhibit A to Nash Affidavit.). Moreover, there was no arbitration agreement entered into between the three parties. (Boles Affidavit, p.2.). Because Financial Security is not a party in this proceeding, the respondent asserts "it is improper to pursue an action to construe this contract when only two of the three parties affected by the ultimate resolution of the issues are within the jurisdiction and participating in these proceedings." (Respondent's Memorandum of Law, p.12.).

The respondent's contention that the reinsurance agreement is actually tripartite in nature is flatly contradicted by the affidavit of Edwin S. Newman, who was present at the time of the contract negotiations. In his affidavit (sworn to January 19, 1968), Mr. Newman avers that "[t]he reinsurance agreement of September 1965 between Hamilton Life Insurance Company and Republic National Life Insurance Company was a separate and distinct agreement between the parties, and there was no concurrent 'parol' agreement apart from said actual reinsurance treaty that the group business reinsured from Hamilton Life to Republic National Life was in turn to be reinsured to a third company [Financial Security] . . ." (p.2).

Moreover, the Hamilton-Republic reinsurance agreement provides:

#### "ARTICLE XIV                  AMENDMENT"

This instrument contains the sole agreement between the parties hereto on the subject of group reinsurance, and it may be amended only by an instrument in writing which expresses such an intention and is signed with the same formalities as this instrument."

The respondent, Republic, has not produced any writing evidencing the so-called tripartite agreement. To allow the respondent to prove that there was an oral agreement modifying the Hamilton-Republic reinsurance agreement would be contrary to the express terms of the agreement and violative of the parol evidence rule. See, *Fogelson v. Rackfay Construction Co.*, 300 N.Y. 334, 340 (1950).

In any event, Financial Security is not an indispensable party to the present proceeding, which is brought not to construe the parties' rights under the reinsurance agreement, but only to enforce the Hamilton-Republic agreement to arbitrate.

The contention that there is no tripartite arbitration agreement joined in by all of the alleged parties—the petitioner (Hamilton), the respondent (Republic) and Financial Security—does not prevent enforcement of the Republic-Hamilton arbitration agreement.

The crucial fact is that the petitioner and the respondent agreed to arbitrate disputes between themselves. There is no impediment to enforcing an agreement to arbitrate entered into between less than all of the parties to a dispute. *Wilko v. Swan*, 201 F.2d 439, 445 (2d Cir.), *rev'd on other grounds*, 346 U.S. 427 (1953); *Lumbermen's Mutual Casualty Co. v. Borden Co.*, 268 F. Supp. 303 (S.D.N.Y. 1967). Whatever claims the respondent may have against Financial Security for indemnification or otherwise do not prevent enforcement of the petitioner's right to compel arbitration under the reinsurance agreement.

The respondent's cross-motion to dismiss for failure to join an indispensable party is denied.

#### IV

The Court concludes that there is no *bona fide* question as to the making and validity of the arbitration agreement and the respondent's "failure to comply therewith." The parties are, therefore, ordered to proceed to arbitration in accordance with the terms of the agreement.

The arbitration clause in the present case is separable from the rest of the agreement and clearly broad enough to cover the defenses raised in the respondent's answer: fraud in the inducement of the contract generally, lack of consideration, failure to comply with conditions precedent, illegality of the subject matter of the contract and breach of contract. Indeed, "it would be hard to imagine an arbitration clause having greater scope than the one before us." *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, *supra*, 271 F.2d at 412. The validity of these claims as well as the question of the respondent's liability to the petitioner will, therefore, be determined by the arbitrators.

The respondent's alternative request that these proceedings be stayed is denied because it has "not made out a clear case of hardship or inequity in being required to go forward . . ." *Landis v. North American Co.*, 299 U.S. 248, 254-255 (1936). A stay of these proceedings would "work damage" to the petitioner,

which has been unsuccessfully attempting to compel arbitration of this dispute for almost one year. Moreover, similar requests that proceedings in this district be stayed have recently been denied by the United States District Court for the District of Arizona, the Ninth Circuit Court of Appeals and the United States Supreme Court. In fact, proceedings in the United States District Court for the District of Arizona have been stayed pending this Court's determination of the motions before it.

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The petitioner's motion to compel arbitration is granted. The respondent's cross-motion to dismiss the petition or, in the alternative, to stay these proceedings is denied.

Settle order on notice in accordance with the views expressed in this opinion.

Dated: New York, N. Y.

July 30, 1968.

WILLIAM B. HERLANDS  
U. S. D. J.

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In the  
**United States Court of Appeals**  
**FOR THE NINTH CIRCUIT**

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No. 22598

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REPUBLIC NATIONAL LIFE INSURANCE COMPANY,  
*Appellant,*  
*v.*

HAMILTON LIFE INSURANCE COMPANY OF NEW YORK and  
FINANCIAL SECURITY LIFE INSURANCE COMPANY,  
*Appellees.*

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**APPELLANT'S REPLY TO BRIEF OF APPELLEES**

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**FILED**

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In the  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

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No. 22598

---

REPUBLIC NATIONAL LIFE INSURANCE COMPANY,  
*Appellant,*  
*v.*

HAMILTON LIFE INSURANCE COMPANY OF NEW YORK and  
FINANCIAL SECURITY LIFE INSURANCE COMPANY,  
*Appellees.*

---

**APPELLANT'S REPLY TO BRIEF OF APPELLEES**

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*To the Honorable Court of Appeals:*

Appellant, Republic National Life Insurance Company, respectfully requests leave to file this its Brief in reply to Brief filed by Appellees.

**I.**

**HAMILTON'S ARGUMENT MISCONSTRUES THE FEDERAL ARBITRATION ACT TO PRECLUDE THE CAUSE OF ACTION ALLEGED IN REPUBLIC NATIONAL'S COMPLAINT AND TO DENY DUE PROCESS OF LAW.**

By characterizing the issues of this case as merely a dispute over the venue of two District Courts under 9 U.S.C.

Sections 3 and 4, Hamilton has obscured the nature of the case. The Complaint alleges a three-party reinsurance contract was formed providing for two successive cessions of insurance. As originating company Hamilton ceded 80 percent to Republic National specifically subject to the prior agreement that Republic National would in turn cede 80 percent (or 64 percent of the original insurance) to Financial Security, to accomplish a division of risk to be borne 20 percent by Hamilton, 16 percent by Republic National, and 64 percent by Financial Security. (See also Boles Affidavit, A.R. 69). By contrast, if Hamilton is permitted to disregard the Complaint and restrict a subsequent adjudication only to Hamilton and Republic National, in the absence of Financial Security, Republic National's potential liability exposure sharply increases to 80 percent of the total, while Hamilton's share of the risk remains constant.

Therefore, without so much as a single ruling on any issue of proof, Hamilton proposes to shut the door to the determination of Republic National's claims stated in the Complaint. Contrary to Hamilton's assurances, the New York forum cannot adjudicate Republic National's claimed right to obtain a determination of its net liability as among the three insurers. (Appellee's Brief p. 7-8). It is no answer to say that in a subsequent proceeding Republic National can attempt to mitigate any loss it sustains through a two-party proceeding. The injustice inherent in such a procedure is that Financial Security could then maintain that the action by Republic National was barred by the absence of Hamilton as an indispensable party.

Any such fundamental restructuring of Republic National's claimed right of recovery, without even the most basic evaluation of the evidence, threatens denial of due process of law. Throughout the recent cases interpreting the Federal Arbitration Act are repeated expressions of concern that considerations of expediency not be allowed to precipitate denials of due process in determining arbitrability. *Bernhart v. Polygraphic Co. of America*, 350 U.S. 198, 76 S. Ct. 273 (1956); *Moseley v. Electronic & Missile Facilities*, 374 U.S. 171, 83 S. Ct. 1815 (1963); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 87 S. Ct. 1801, 1808 (1967); *Collins*, Arbitration and the U.C.C., 41 N.Y.U. L. Rev. 736 (Oct. 1966); *Bernstein*, The Impact of the U.C.C. Upon Arbitration; Revolutionary Overthrow or Peaceful Existence, 42 N.Y.U. L. Rev. 8 (March 1967); Scope of the U. S. Arbitration Act in Commercial Arbitration: Problems in Federalism, 58 Northwestern U. L. Rev. 468 (Sept.-Oct. 1963); Judicial Control of the Arbitrators Jurisdiction: A Changing Attitude, 58 Northwestern U. L. Rev. 521 (Sept.-Oct. 1963); *Kronstein*, Arbitration is Power, 38 N.Y.U. L. Rev. 661 (June 1963). The corollary to this is the Court's requirements that stays under 9 U.S.C. Section 3 be determined upon decided fact. *Engineers Assoc. v. Sperry Gyroscope Co.*, 251 F. 2d 133 (2d Cir. 1957); *Kulukundis Shipping Co. v. Amtorg Trading*, 126 F. 2d 978, 988 (2d Cir. 1942); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 87 S. Ct. 1801 (1967). This in turn prevents parties, such as Republic National, from being stripped of their justiciable controversies without hearing, as Hamilton now appears content to do.

In this light the *Kerotest* doctrine (Appellant's Brief pp. 23-28) is more than a mere aid to efficient judicial administration; rather it is the cornerstone of due process. Ignoring it as Hamilton proposes would bar for all time Republic National's attempts to establish the three-party contractual arrangement pleaded in its Complaint. On the other hand, if by reliance on the *Kerotest* doctrine the procedural cart and horse are put back in proper order, the nature of the contract and the parties' relationships with respect to arbitration can be determined by applying the law to the facts placed of record. Then, if under the facts the District Court is " \* \* \* satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, \* \* \* it may stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement. \* \* \*" 9 U.S.C., Section 3.

Republic National is as entitled to have an equal opportunity to show that the issue involved in this action is not referable to arbitration as Hamilton is to show the opposite. This can only be accomplished by resolving questions of fact. But to date every such effort has been disregarded in deference to the Hamilton theory that arbitration agreements outweigh all considerations of fact and relevancy. (See Motion for Partial Summary Judgment, A.R. p. 63). Instead, with respect to the Court's duty in passing on stays requested under 9 U.S.C., Section 3, it is said:

"In construing the provisions of the Federal Arbitration Act, we have stated that after determining that the parties have entered into an arbitration agreement,

the duty of the court is to determine 'whether any of the issues raised in the suit were within the reach of that agreement.' Kulukundis Shipping Co. v. Amtorg Trading Corp., 2 Cir., 1942, 126 F. 2d 978, 988. This duty cannot be adequately performed unless the court examines the facts upon which the demand for arbitration is based as those facts relate to the language of the agreement." Engineers Ass'n. v. Sperry Gyroscope Co., etc., 251 F. 2d 133, 137 (2d Cir. 1957).

## II.

### **NO DISCRETIONARY STAY WAS GRANTED BY THE DISTRICT COURT.**

Hamilton has branded the order appealed from as *prima facie* invalid by attempting to support the order by a rationale inconsistent with the District Court's. The Court stated:

"The Court has considered plaintiff's motion for rehearing and in the alternative for stay pending appeal. The Court has reviewed again the various memoranda submitted by both parties and the authorities cited therein. The Court is still convinced that the whole statutory scheme of proceedings provided for in the Federal Arbitration Act contemplates that under a procedural situation such as in this case, this Court being satisfied that on the face of the pleadings there is a written contract involving commerce with disputed issues under the contract that come within the scope of the arbitration clause contained in the contract, defenses (factual and legal) to a charge of refusal to arbitrate should be heard and determined in connection with the petition to compel arbitration pending in the District where arbitration is contemplated by the terms of the contract." A.R. p. 101.

Rather than to show a basis in law for this order under 9 U.S.C., Section 3, Hamilton states that the Court *could*

have achieved the same result by an exercise of discretion. (Appellee's Brief, Point III). To reach this result one must first totally ignore the record. Hamilton's original Motion for Stay of Proceedings Pending Arbitration (A.R. p. 10) bases its request on 9 U.S.C., Section 3 (Motion p. 3, A.R. p. 12). Subsequently, in its Memorandum in Support of Motion for Stay, Hamilton set forth the discretionary stay theory. (A.R. p. 41). Then, the discretionary stay concept was argued to the Court in the January 8, 1968 hearing. (Transcript, p. 20, l 23-21, l 11; p. 23, l 21-24, l 16). At that hearing the Court stated:

"The thing that concerns me, Mr. Frank, on which I am going to do a little more work is that I don't see that this court can grant a stay pursuant to a particular statute unless it first implicitly finds that the statute applies." (Transcript, p. 22, l 7-11).

It is obvious that no considerations of discretion entered into the orders appealed from which clearly relates only to 9 U.S.C., Section 3.

Also, justifying the order upon the grounds of discretion is abhorrent to logic. Carried to its logical ends, Hamilton's argument means that no stay entered in reliance on 9 U.S.C., Section 3, no matter how misconceived, would constitute reversible error. The precedents are to the contrary. *Ets-Hokin & Galvan, Inc. v. United States ex rel. Albert S. Pratt, Inc.*, 350 F. 2d 871 (9th Cir. 1965); *American Safety Equipment Company v. J. P. McGuire & Co.*, 391 F. 2d 821 (2d Cir. 1968);

Nor can a Court discreetly achieve a result which is contrary to due process of law as previously discussed. The concept of the abuse of judicial discretion is discussed in *Martin v. Graybar Electric Company*, 266 F. 2d 202, p. 204:

"Two simultaneously pending lawsuits involving identical issues and between the same parties, the parties being transposed and each prosecuting the other independently, is certainly anything but conducive to the orderly administration of justice. We believe it to be important that there be a single determination of a controversy between the same litigants and, therefore, a party who first brings an issue into a court of competent jurisdiction should be free from the vexation of concurrent litigation over the same subject matter, and an injunction should issue enjoining the prosecution of the second suit to prevent the economic waste involved in duplicating litigation which would have an adverse effect on the prompt and efficient administration of justice unless unusual circumstances warrant. As none such appears in this record, we agree with what would seem to be the established general rule that the party filing later in time should be enjoined from further prosecution of his suit. Milwaukee Gas Specialty Co. v. Mercoid Corporation, 7 Cir., 1939, 104 F. 2d 589, 592; Crosley Corporation v. Hazeltine Corporation, 3 Cir., 1941, 122 F. 2d 925, 929; Cresta Blanca Wine Co. v. Eastern Wine Corporation, 2 Cir., 1944, 143 F. 2d 1012, 1014; Independent Pneumatic Tool Co. v. Chicago Pneumatic Tool Co., 7 Cir., 1948, 167 F. 2d 1002, affirming D.C., 74 F. Supp. 502; Speed Products Co. v. Tinnerman Products, 1948, 83 U.S. App. D.C. 243, 171 F. 2d 727, 730."

Since Hamilton can perceive no justification for the Court's order on its face, it should be reversed.

## III.

**THE McCARRAN QUESTION.**

Hamilton argues that the McCarran Act has been narrowly limited in its application. The scheme of the McCarran Act was to provide that insurance companies be subject to state law and not federal law unless that federal law was specifically made applicable to the business of insurance. The Act does not require the presence of a precise and specific state statute relating solely to insurance companies in order to defeat federal supremacy. The Act, in Section 2(a) and (b), calls for federal subordination, subject to certain exceptions contained in Section 4. On this question it is interesting to note the debate contained in the Congressional Record as follows:

“Mr. RADCLIFF. I agree with the Senator from Utah that the statement in subsection (a) of section 2 is quite definite and clear. But it has seemed to those who have been working upon this bill that there was some need or at least advisability that there should not be any repeal by implication. The statement beginning on page 1 is a general statement setting forth the purposes.

“Since there seems to be doubt in the minds of certain people that there might be repeal by implication or that a general statement might have some crimping effect, it would not be at all unusual if a saving clause were put in the bill. It may not be necessary, but in the spirit of caution I think it might be desirable, especially knowing the very serious problems which have been confronting the insurance companies and the various States to leave them free to meet conditions some of which cannot now be foreseen. \* \* \*”

"Mr. O'MAHONEY. Does not subsection (a) of section 2 take complete account of that fact, and grant complete protection to existing State laws?

"Mr. FERGUSON. I agree that, as to existing State laws, subsection (a) of Section 2 does so provide.

"Mr. O'MAHONEY. Let me read it: 'The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.' That is complete.

"Mr. FERGUSON. I think that is correct.

"Mr. O'MAHONEY. There is no reason for misunderstanding on the part of any State official or any insurance company or any policyholder with respect to the meaning of that subsection as it applies to existing law.

"Mr. FERGUSON. As it applies to existing law, that is correct. However, subsection (b) provides for something further. It provides that no Federal legislation relating to interstate commerce shall by implication repeal any existing State law unless such act of Congress specifically so provides.

"Mr. O'MAHONEY. The Senator puts his finger upon the precise center of this dispute, or misunderstanding. Let me say to the Senator that, recognizing the complexity of this problem, and the desirability of maintaining State regulation and State taxation, members of the Judiciary Committee who were opposed to the proposal to grant a blanket exemption from the antitrust laws desired to go as far as was humanly possible in the direction of giving the States a clearcut opportunity to adjust State laws in accordance with Supreme Court decisions and the antitrust laws.

"It is no secret that Senate Bill 12, introduced by the Senator from New Mexico (Mr. Hatch) and myself, and Senate Bill 340, the bill which was reported by the committee, are modifications of a measure which

was originally drafted by the legislative committee of the National Association of Insurance Commissioners. So there was an effort to work with those groups. In drafting those two bills we sought to spell out each particular law which might apply to insurance. We referred specifically to the Federal Trade Commission Act, the Robinson-Patman Act, the National Labor Relations Act, and the Fair Labor Standards Act. In other words, a good-faith attempt was made to specify every single law which had an application or might have an application, to insurance.

"Section 2(b) was drafted and written into the bill which I introduced, in the belief, not that it would be interpreted as an additional exemption from the anti-trust laws, but that it would be a sort of catch-all provision to take into consideration other acts of Congress which might affect the insurance industry, but of which we did not have knowledge at the time. \* \* \*" Congressional Record-Senate, January 25, 1945, Page 483.

The limits on McCarran have been applied in areas where exceptions were imposed, such as the Clayton Act and the Robinson-Patman Act, *U. S. v. Chicago Title & Trust Co.*, 242 F. Supp. 56 (N.D. Ill. 1965), and the Federal Trade Commission cases cited in Appellant's Original Brief. This Congressional intent has recently been displayed by the precise provisions for including insurance companies in the application of Securities Regulation Statutes, as evidenced by the 1964 Amendments referred to in the opinion of this Honorable Court in the National Security case.

Apart from these considerations, Hamilton appears to seek affirmance of the Arizona orders on the ground that the

damage has already been done through decision of the two-party issues in New York. However, the issue here is fundamental jurisdiction, and the error of the Arizona Court is only enlarged by the furtherance of the bilateral proceedings in derogation of Republic National's preexisting and preeminent right to have the proceedings on the issues framed by its Complaint pursued. Questions of conflicts of laws, indispensable parties, and contested issues of fact discussed in the opinion of the New York Court can be considered upon their merits in the due course of that action. They are no part of this record on appeal and cannot now be properly discussed here.

## CONCLUSION

The orders of the District Court are not supported by 9 U.S.C., Section 3, although clearly issued in reliance upon the statute. Hamilton bases its hopes for affirmance only upon discretion which cannot be exercised contrary to the requirements of the statute. To accept the Hamilton position would negate basic concepts of due process which have long been of concern in interpreting the Federal Arbitration Act. The McCarran Act, both as interpreted by the Court and as established by its legislative history, demonstrates an intention to exempt the insurance business from the Federal Arbitration Act. Therefore, this case should be re-

manded to the District of Arizona with instructions to proceed with a determination of the issues pursuant to that exemption.

Respectfully submitted,

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Copies of the foregoing Brief have been served by mail this  
21 day of May, 1968, upon Mr. John P. Frank of  
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pellees.

*T. G. Nash*

UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

MAR 10 1969

REPUBLIC NATIONAL LIFE INSURANCE  
COMPANY,

Appellant,

v.

HAMILTON LIFE INSURANCE COMPANY OF  
NEW YORK and FINANCIAL SECURITY  
LIFE INSURANCE COMPANY,

Appellees.

No. 22598

APPELLANT'S SUPPLEMENTAL BRIEF  
REGARDING JURISDICTION

FILED

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IN THE  
UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

REPUBLIC NATIONAL LIFE INSURANCE  
COMPANY,

Appellant,

v.

HAMILTON LIFE INSURANCE COMPANY  
OF NEW YORK and FINANCIAL SECURITY  
LIFE INSURANCE COMPANY,

Appellees.

No. 22598

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APPELLANT'S SUPPLEMENTAL BRIEF  
REGARDING JURISDICTION

---

During the argument of this case on January 7, 1969, members of the Court requested supplemental memoranda to be submitted simultaneously by both counsel showing whether the requirements of federal jurisdiction exist.

The controversy, as stated in plaintiff's complaint, and amplified by the various exchanges of memoranda, briefs, and in argument, consists of two counts. The first is for declaratory judgment setting forth the respective rights and liabilities of Republic National, Hamilton and Financial Security as participating insurers in the reinsurance contract described in the complaint, including a declaration that Republic National is not liable as a reinsurer because of failure of consideration and fraud in the inception. In the alternative, it is requested that declaratory judgment be



entered determining the extent of respective liability of the three insurers for the total claim of \$347,529.26 of insurance claims allegedly made upon the subject insurance policies.

As stated in Republic National's brief, the dispute is essentially whether of the total claims, Republic National is liable for 80% (\$278,023.41), as claimed by Hamilton, or for 16% (\$55,604.68) as contended by Republic National, with the remaining 64% liability (\$222,418.73) to be borne by Financial Security.

In the second count of the complaint, Republic National alleges that by reason of its breach of contract Hamilton has damaged Republic National in the sum of \$60,000.00.

Declaratory judgment relief is requested under the jurisdiction conferred upon the Court by 28 U.S.C. § 2201. In order to obtain such a judicial construction of the parties' liability under an insurance contract, it is necessary for three elements of federal jurisdiction to co-exist. First, there must be diversity of citizenship. Second, there must be an actual controversy between the parties to the action. Third, the statutory minimum amount in controversy must be present.

C. E. Carnes & Co. v. Employers' Liability Assurance Corp., C.C.A.5 1939, 101 F.2d 739, 741. Each of these requirements exists in the present action as demonstrated below.

It is well settled that an action by an insurer to establish the extent of its liability is an actual controversy sufficient to vest jurisdiction in the Court. Aetna Life Insurance Co. v. Haworth, 300 U.S. 227, 57 S.Ct. 461,



81 L.Ed. 617 (1937). There, the Supreme Court stated that the character of the controversy and of the issue to be determined is essentially the same whether it is presented by the insured or by the insurer. "It is the nature of the controversy, not the method of its presentation or the particular party who presents it, that is determinative." Aetna Life Insurance Co. v. Haworth, supra, 244, 465.

Interpreting the Aetna Life Insurance Co. v. Haworth case, the Court of Appeals for the Eighth Circuit stated:

"That decision holds in effect that where under an insurance policy the insured has a right of action against the insurer, the insurer has a corresponding right to maintain a suit under the Declaratory Judgment Act to secure a judgment determining the obligations and liabilities of the parties." Aetna Life Insurance Co. v. Williams, C.C.A. 8<sup>1</sup> 1937, 88 F.2d 929, 930.

Likewise, in a suit to construe liability under group insurance contracts, it has been held that when those insured by the policy are asserting liability of the company and the company is denying liability claiming the policy is terminated, the suit involves a real and substantial controversy for determination by declaratory judgment. Anderson v. Aetna Life Insurance Co., C.C.A. 4 1937, 89 F.2d 345, 347.

Therefore, applying these standards to the present case, where Republic National has been presented with insurance claims totalling \$278,023.41 which it denies it owes, or at most owes only partially, and has instituted an action against its coinsurers for a determination of their respective liabilities, the requirement for an actual justiciable



controversy has been satisfied.

The next question is whether the allegations of Republic National's complaint show the minimum jurisdictional amount in controversy of \$10,000.00 required by 28 U.S.C. § 1332. In making this determination, the allegations of the complaint are to be taken as stating the amount in controversy, unless it appears to a legal certainty that the claim is really for less than the jurisdictional amount. Horton v. Liberty Mutual Insurance Co., 367 U.S. 348, 81 S.Ct. 1570, 1573 (1961). No party has questioned the good faith of Republic National's allegations in its complaint.

Taking the most conservative view of the complaint, that the amount in controversy is the difference between the maximum amount claimed by Hamilton and the maximum liability foreseen by Republic National, the resulting differential is \$222,418.73. This is in accord with the standard for fixing jurisdictional amounts stated in Davis v. American Foundry Equipment Co., C.C.A.7 1938, 94 F.2d 441. There it was stated that the jurisdictional amount in contract cases for declaratory judgment is to be determined by the amount which it is sought to have declared free from doubt, that is the difference between what plaintiff and defendant each claim is due and owing. By this standard, the \$10,000.00 minimum has been amply satisfied in this instance, whether under this standard the amount in controversy is viewed as being \$347,529.26, \$278,023.41, or \$222,418.73.

It has also been stated that the jurisdictional amount



in controversy is established where there is an actual controversy over contractual rights, whether contingent or liquidated. Hardware Mutual Casualty Co. v. Schantz, C.C.A.5 1949, 178 F.2d 779.

There is no apparent concern over the diversity of the parties in this case. The Plaintiff, Republic National, is a Texas corporation, with its principal place of business at Dallas, Texas. The Defendants Hamilton and Financial Security are New York and Arizona corporations, respectively, neither of whom has alleged a principal place of business in Texas. Therefore, total diversity of citizenship exists.

#### CONCLUSION

The three requirements for the exercise of declaratory judgment jurisdiction are present in this case. An actual controversy exists to determine how the liability for \$347,529.26 is to be apportioned between the three insurers who are parties to this action, which should be determined by an action for declaratory relief.

Respectfully submitted,

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A copy of the foregoing Supplemental Brief has been served by mail this 13th day of January, 1969, upon Mr. John P. Frank of the firm of Lewis, Roca, Beauchamp & Linton, 114 West Adams Street, Phoenix, Arizona 85003, Attorneys for Appellees.

Robert H Zollana



IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

EDWARD STANLEY WADLEY, )  
Appellant, )  
vs. ) No. 22599  
PEOPLE OF THE STATE OF CALIFORNIA, )  
LOUIS S. NELSON, Warden, )  
San Quentin State Prison, )  
Appellees. )

---

APPELLEES' BRIEF

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U.S. DISTRICT COURT



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IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

EDWARD STANLEY WADLEY, )  
Appellant, )  
vs. ) No. 22599  
PEOPLE OF THE STATE OF CALIFORNIA, )  
LOUIS S. NELSON, Warden, )  
San Quentin State Prison, )  
Appellees. )  
\_\_\_\_\_  
)

APPELLEES' BRIEF

JURISDICTION

The jurisdiction of the United States District Court to entertain appellant's petition for writ of habeas corpus was invoked under Title 28 United States Code section 2241. The jurisdiction of this Court is conferred by Title 28, United States Code section 2253, which makes an order in a habeas corpus proceeding reviewable in the Court of Appeals when, as in this case, a certificate of probable cause has issued.

STATEMENT OF THE CASE

Appellant is appealing from an order of the United States District Court for the Northern District of California denying his petition for writ of habeas corpus.

A. Proceedings in the State Courts.

On February 5, 1963, appellant was convicted of a violation of section 11530 of the California Health



1/  
and Safety Code, a felony (TR 57). On February 19, 1965, appellant was placed on parole (TR 115). He was thereafter on March 22, 1966, convicted of robbery in violation of California Penal Code section 211 and further found to have suffered the prior felony conviction (TR 58). By a report filed on March 25, 1966, appellant was charged with three violations of his parole agreement: (1) That he violated the conditions of his parole by committing robbery as evidenced by the conviction for that crime. (2) That he violated the conditions of his parole by having an automatic pistol in his possession. (3) That he violated the conditions of his parole by associating with parolees and numerous other persons of ill repute in the community (TR 170-173). On March 31, 1966, appellant's parole was cancelled (TR 168, 169). Petitioner appealed the robbery conviction to the California Court of Appeal, and said conviction was affirmed on April 27, 1967 (TR 30-39). Appellant did not file habeas corpus petitions in the state courts raising the issues presented to this Court, but rather made his initial application for habeas corpus relief in the federal courts (TR 5, 11, 54-55).

B. Proceedings in the Federal Courts.

On September 27, 1966, the Honorable Alfonso J. Zirpoli, Judge of the United States District Court ordered

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1. "TR" refers to the transcript of record of the proceedings in the District Court.



that appellees file a return to the petition for habeas corpus which appellant had filed on July 13, 1967 (TR 1-11, 42). On October 20, 1967, appellees filed its return to said order to show cause, with accompanying exhibits (TR 53-59).

On November 14, 1967, the Honorable Alfonso J. Zirpoli caused to be filed an order directing appellees to make further return setting forth (1) whether and how petitioner's present confinement is in any way affected by his conviction of February 5, 1963, and (2) appellees' arguments on the merits of the petition for writ of habeas corpus (TR 74). The further return to the order to show cause and points and authorities in opposition pursuant to this order was filed by appellees on December 4, 1967 (TR 158-174).

The order denying the petition for writ of habeas corpus, discharging the order to show cause and dismissing the proceedings, signed by the Honorable Alfonso J. Zirpoli was filed on December 14, 1967 (TR 188-190). Notice of appeal was thereafter filed by appellant on January 31, 1968, however, the day preceding, the Honorable Alfonso J. Zirpoli issued an order granting a certificate of probable cause because "This Court finds that an appeal, to determine whether Arketa v. Wilson, 373 F.2d 582 (9th Cir. 1967) applies to the facts of this case,

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would not be frivolous," (TR 200).<sup>27</sup> Appellant's opening brief was received in appellees' office on April 3, 1968.

#### APPELLANT'S CONTENTIONS

1. The District Court erred by not allowing appellant to traverse appellees' further return.

2. Appellant's confinement under the 1963 conviction would have expired had appellant not been illegally convicted in the 1966 proceeding now in question.

3. Appellant is in custody in violation of the United States Constitution and has no other remedy other than federal habeas corpus for relief.

#### SUMMARY OF APPELLEES' ARGUMENT

I. The court's failure to allow petitioner to traverse appellee's further return was not error, because 28 United States Code section 2243 does not guarantee to a habeas corpus applicant the right to traverse every pleading.

II. The District Court's finding that appellant's parole was revoked for cause independent of the 1966 conviction is supported by the record.

III. The instant petition does not come within the rule stated in Arketa v. Wilson.

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2. Appellant's notice of appeal was received by the Clerk of the United States District Court on January 12, 1968, two days before the expiration of the 30-day period allowed by 28 United States Code, section 2107 and Rule 73(a), Federal Rules of Civil Procedure, however, it was not filed until January 31, 1968, one day after the District Court granted a certificate of probable cause. We surmise that the delay was not occasioned through the fault of appellant and for that reason, we do not press the timeliness issue.



ARGUMENT

I

THE COURT'S FAILURE TO ALLOW PETITIONER TO TRAVERSE APPELLEE'S FURTHER RETURN WAS NOT ERROR, BECAUSE 28 UNITED STATES CODE SECTION 2243 DOES NOT GUARANTEE TO A HABEAS CORPUS APPLICANT THE RIGHT TO TRAVERSE EVERY PLEADING.

The applicable part of 28 United States Code section 2243 states:

"The applicant or the person detained may, under oath, deny any of the facts set forth in the return or allege any of the material facts."

The word "may," of course, denotes a permissive condition and not a mandatory one. Solenoid Devices, Inc. v. Ledex, Inc., 375 F.2d 444, 445 (9th Cir. 1967). Appellant did traverse appellee's return to the order to show cause (TR 75-83). His only complaint is that he was not able to traverse the further return. A District Court may permit any of the parties to file supplemental pleadings - even after the writ has been granted, Gladden v. Gidley, 337 F. 2d 575, 577-578 (9th Cir. 1964) but there is no requirement that the opposing party be allowed to traverse. Furthermore, the writ was denied on a point of law rather than upon a factual determination going to the merits of the petition (TR 188-190). Therefore, a traverse to the further return was not only unnecessary, but it could have no influence whatsoever upon the ultimate resolution of the question of law presented.



II

THE DISTRICT COURT'S FINDING THAT APPELLANT'S PAROLE WAS REVOKED FOR CAUSE INDEPENDENT OF THE 1966 CONVICTION IS SUPPORTED BY THE RECORD.

Appellant's second argument (AOB 15-19), his heading notwithstanding, consists of an attack upon the factual basis of the parole officer's report upon which his parole was revoked. It is immaterial whether the facts did or did not exist as appellant suggests. What is material is that the revocation did occur as a result of this report - i.e., for cause shown. See Cal. Pen. Code § 3063, In re Costello, 262 F.2d 214, 215 (9th Cir. 1958); In re McLain, 55 Cal.2d 78, 87; 357 P.2d 1080 (1960). The fact that appellant was found guilty of the three charges, and that they constituted "cause" is all that is important to this Court. In re Costello, supra.

III

THE INSTANT PETITION DOES NOT COME WITHIN THE RULE STATED IN ARKETA V. WILSON.

The District Court granted a certificate of probable cause to determine whether Arketa v. Wilson, 373 F.2d 582 (9th Cir. 1967) applied to this case (TR 200). Appellant's final argument (AOB 19-22) is to the effect that this case does come within Arketa because, absent the 1966 conviction, he allegedly would be eligible for parole "immediately" (AOB 20).

Arketa does not aid appellant. That case involved a situation wherein the petitioner was attacking



the validity of his prior conviction. Against a McNally argument (McNally v. Hill, 293 U.S. 131 (1934)), this Court found that but for the prior conviction, petitioner would have been eligible for probation at the time of sentencing on the second conviction, and thus, petitioner should be allowed to attack the prior in federal habeas corpus. 373 F.2d 585. The court noted that in Martin v. Commonwealth of Virginia, 349 F.2d 781 (4th Cir. 1965) a similar step was taken in relation to a prisoner who claimed that, but for the invalid prior conviction, he would be eligible for parole under the later conviction. The court decided not to go so far, because in order to do so, it would, as did the Fourth Circuit, have to cast McNally aside with the rather presumptuous and illogical reasoning that if McNally were heard by today's Supreme Court, it would be decided differently. 373 F.2d 585. Appellant herein asks this Court to take that step and splinter the doctrine of stare decisis (AOB 20). This Court would not do so in Arketa, and it should not do so here.

We point to this language in Arketa, which quotes McNally:

"The petitioner asks here only a ruling which will establish his eligibility for parole, because of the invalidity of the sentence on the third count. The ruling sought is such as might be obtained in a



proceeding brought to mandamus the parole board to entertain his petition for parole, if the sentence on the third count were void for want of jurisdiction of the court to pronounce it. This use of habeas corpus is unauthorized by the statutes of the United States\* \* \*'" 373 F.2d at 584.

We submit that this language adequately disposes of appellant's desire to stretch the ruling of Arketa in reference to probation eligibility, to one in which the question presented is parole eligibility.

Appellant seeks to further distinguish this case from McNally by declaring that, unlike the federal petitioner therein, he does not have another remedy available to him (AOB 21). However, this appellant does have another remedy, Arketa v. Wilson, supra, 373 F.2d 585, 584, fn. 4, which he has specifically and intentionally by-passed (TR 5, 11, 54-55). Appellant hardly has presented his case in a posture conducive to the granting of the highly extraordinary relief he seeks. Cf. Walker v. Wainwright, 36 U.S.L.Week 3357 (1968).

Finally, we must note that the Martin case's spawn, Peyton v. Rowe and Peyton v. Thacker are presently before the United States Supreme Court. The continuing validity of McNally is the question before the court. We surmise that this Court may deem it propitious to await the outcome of that case before deciding this one.



However, for the present time, suffice it to say that the decision of the District Court in the light of prevailing law is manifestly correct. Ex Parte Hull, 312 U.S. 596 (1941) does not apply because appellee's parole was revoked for reasons other than the 1966 conviction. The lower court so found; the record supports that finding. Because of the prior, uncontested conviction, McNally v. Hill applies, and the order denying the writ so acknowledges that fact (TR 188-189). That order should be affirmed.

#### CONCLUSION

For the foregoing reasons, we respectfully submit that the judgment of the District Court should be affirmed.

DATED: April 26, 1968

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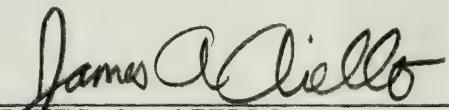
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CERTIFICATE OF COUNSEL

I certify that in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit and that in my opinion this brief is in full compliance with these rules.

DATED: April 26, 1968

  
JAMES A. AIELLO  
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